The Southland Corporation Annual Report -- 1992
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The Southland Corporation

1992 Annual Report

In 1992 Southland initiated many changes that have begun to improve 7-Eleven customer service and profitability — most notably a new merchandising process and an ambitious store remodeling program.

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COMPANY PROFILE

History

The convenience retailing industry began in 1927 when a Southland Ice Company employee met the needs of his customers by selling bread, milk and eggs from the steps of his ice dock. Today the company is the largest operator, franchisor and licensor of convenience stores in the world, with more than 13,700 stores in 20 countries carrying the 7-Eleven banner. (See inside back cover for listing of stores by country and by state.) With $7.48 billion in 1992 revenues, Southland is the 15th largest retailer in the United States.

IYG Holding Company (IYG) owns 64 percent of Southland's common stock. IYG is 51-percent owned by Ito-Yokado Co., Ltd., the fifth largest retailer in the world, and 49-percent owned by Seven-Eleven Japan Co., Ltd., the longtime 7-Eleven licensee for Japan, which opened its 5,000th store in February 1993.

Southland's common stock is traded on the Nasdaq Small-Cap Market under the ticker symbol SLCMC.

Southland and the Convenience Store Industry

The convenience retailing industry entered a new phase in the mid-1980s, when major oil companies began to accelerate the conversion of their corner gasoline stations to convenience stores. Although the units operated by the oil companies and their dealers focused primarily on gasoline sales, the sheer number of their locations and their extensive financial resources transformed the competitive nature of the entire convenience store business within a few years.

In March 1991, Southland completed a four-month Chapter 11 reorganization, the result of burdensome debt incurred in a 1987 leveraged buyout. Through the reorganization, the company was able to restructure its public debt and obtain a necessary capital infusion from IYG. Since emerging from bankruptcy, the company has begun a total reformation of its convenience retailing operations. Because of customer awareness of the 7-Eleven name, Southland's large and geographically dispersed store base, the dedication of its employees, franchisees and licensees, and the financial strength of its majority owners, Southland is positioned to greatly increase the appeal of its stores to customers.

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COVER PHOTO: Approximately 1,300 7-Eleven stores will be remodeled in 1993 to the standards of this prototype: increased interior and exterior lighting, a standardized three-stripe facade, appealing open-front fresh food display cases, a more convenient and less cluttered store layout with improved signage, and upgraded gasoline equipment at stores that sell gasoline. Southland would like to complete the remodeling of its store base by the end of 1996.

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FINANCIAL HIGHLIGHTS

(Dollars in Millions, Except Per-Share Amounts)	1992	1991	1990	1989
FOR THE YEAR:				
Net Sales	$ 7,425.8	$ 8,009.5	$ 8,347.7	$ 8,274.9
Other Income	51.3	66.5	62.4	77.0
Total Revenues	7,477.1	8,076.0	8,410.1	8,351.9
Net Earnings (Loss)(1)(2)	(131.4)	82.5	(276.6)	(1,306.9)
Net Earnings (Loss) Per Common Share(1)(2)	(.32)	.24	(13.93)	(64.76)
Capital Expenditures	88.6	69.9	39.6	105.2
Interest Expense(2)	123.6	189.3	459.5	572.2
AT YEAR-END:				
Common Shares Outstanding (in thousands)	410,022	410,022	20,481	20,504
Number of Stores Operated or Franchised by Southland in U.S. and Canada	6,167	6,491	6,705	6,920
Number of Stores Operated by Licensees or Affiliates in U.S. and Overseas	7,593	6,995	6,436	5,876
Shareholders of Record(3)	3,373	3,314	22	23
Number of Employees (Full-time and Part-time)	35,646	42,616	45,665	48,114
Shareholders' Equity (Deficit)(2)	$ (1,319)	$ (1,210)	$ (1,999)	$ (1,716)
Book Value per Common Share(2)	(3.22)	(2.95)	(97.58)	(83.68)
Total Assets	2,045	2,612	2,814	3,446

(1) Net earnings (loss) for the years presented include the following:	1992	1991	1990	1989
Loss on non-store assets sold(4)	$ (45.0)	—	$ (41.0)	—
Write-off (noncash) of excess of cost over fair value of net assets acquired	—	—	—	$ (947.0)
Earnings from discontinued operations	—	—	—	69.4
Gain on debt restructuring	—	$ 156.8	—	—
Tax benefit from utilization of net operating loss carryforwards	—	—	52.0	—
Charge resulting from debt exchange	—	—	—	(56.0)
Cumulative effect of accounting change for postretirement medical benefits	—	—	(27.2)	—
Severance and related costs	(17.5)	—	—	—
Gain (loss) on closings and divestitures of stores(4)	(34.5)	(4.4)	(10.1)	35.6

(2) The company is required to prepare its financial statements since completing its reorganization in accordance with Statement of Financial Accounting Standards No. 15 (SFAS No. 15). Under SFAS No. 15, the liability for the company's restructured public debt as recorded on the balance sheet includes all future undiscounted cash payments, both principal and interest. For that reason, no interest expense will be recognized over the life of these securities, although the interest payments are tax deductible. The liability is reduced by the amount of the interest payments at the time they are disbursed. Those cash interest payments, which are paid semiannually, totaled $97 million during 1991 and $65 million in 1992, and will total $65 million annually from 1993 through 1996, after which payments will decline because of bond maturations.

(3) The common stock began trading publicly on March 5, 1991, when the company emerged from bankruptcy.

(4) Includes completed closings and divestitures, as well as those expected in the near future.

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TO OUR SHAREHOLDERS AND BONDHOLDERS:

During 1992 we took decisive actions to improve 7-Eleven customer service and restore us to future profitability and growth. Among the most significant changes of the last year, we:

— began to implement in 7-Eleven stores nationwide a new merchandising process that we call Accelerated Inventory Management (AIM), which has increased sales and profitability in those stores where it is being applied to a significant number of product categories;

— introduced a new retail pricing strategy that includes the phase-out of discounting and price promotions and a transition to "everyday fair pricing" on all products;

— removed management layers and streamlined our organization to improve communication and lower our expenses by approximately $50 million annually;

— began the most ambitious store upgrade program in our history, with approximately 1,300 stores scheduled for remodeling in 1993;

— sold or closed our own distribution and food processing facilities, so that our only focus is convenience retailing;

— signed a service agreement with McLane Company, Inc., the country's largest convenience store distributor, by which we expect to lower 7-Eleven costs and improve service;

— reduced our senior bank debt by $492.0 million to $237.9 million and obtained a modification in covenants enabling us to make long-range capital expenditure plans;

— obtained a commercial paper facility of up to $400 million (at interest rates approximately 2.5 percentage points below our senior bank debt), which received the highest credit ratings due to the backing of one of our majority owners, Ito-Yokado Co., Ltd. (Commercial paper outstanding at year-end was $221.9 million.)

These actions began to improve our operating profitability in the second half of 1992. Some of the changes, however, resulted in up-front or nonrecurring costs that were a major factor in the company's 1992 net loss of $131.4 million. The loss included a $45.0 million charge on the disposition of our distribution business; $17.5 million in severance and related costs; a loss of $17.0 million for the sale or planned divestiture of some 225 stores in 1992 and 1993; and a $17.5 million charge for the closing of unprofitable stores in 1992 as well as planned 1993 store closings. Due to a $156.8 million extraordinary gain on the company's bond debt restructuring, earnings of $82.5 million were reported in 1991.

Revenues of $7.48 billion for 1992 were down 7.4 percent from 1991 due to about 260 fewer convenience stores, the inclusion of only eight months of outside sales for our distribution and food centers and lower same-store merchandise sales.

To eliminate customer confusion, in 1992 7-Eleven began shifting to an "everyday fair price" strategy, which greatly reduced discounting and promotional activity. As a result, the company lost some sales from people who had been selectively shopping 7-Eleven stores for the lowest prices on beer, soda and cigarettes. This contributed to a decline in same-store (stores open more than a year) merchandise sales of 3.9 percent for the year. The company expects its new inventory management process, including the aggressive introduction of new products, to gradually improve sales trends. Many other aspects of our 7-Eleven operations, such as gross profit margins and gasoline gallonage, met or exceeded our expectations for 1992, and continued to be very strong in early 1993. (See Operations Review beginning on page 4.)

Our new AIM process is the company's most exciting merchandising approach in decades. A total change in the way we merchandise our stores, AIM is *not* an inventory reduction program, although that has been a side benefit. AIM is also not a one-time "fix" of our store product mix, but a complex, ongoing process. Our majority owners, Ito-Yokado Co., Ltd., and Seven-Eleven Japan Co., Ltd., have *steadily* improved their per-store productivity since implementing a proprietary procedure similar to AIM more than a decade ago.

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AIM shifts ordering responsibility to the store staff and emphasizes item-by-item sales forecasting; ongoing deletion of slow-moving items; flexible and continuously improving store layouts; and, importantly, the weekly addition of new products, including those new to the marketplace. This represents a radical departure from our old policy of not stocking items until they had achieved a certain market share, which deprived our stores of the "growth phase" of many products' life cycles. 7-Eleven's merchandise variety will improve over time as we gradually add hundreds of items at each store.

We've already seen proof that AIM performed without electronic point-of-sale equipment (EPOS) can produce positive results, because the most critical element of sales forecasting is the store staff's judgment and customer knowledge. While our goal is to achieve total automation of the 7-Eleven store information system, as a first step we will begin the installation of backroom computers in 1993. This will automate certain accounting tasks and give store operators more time to concentrate on customer service. Meanwhile, we will continue to refine the ordering and sales forecasting processes that eventually will be facilitated by EPOS.

We are often asked about the role of convenience stores in an era dominated by low-price, high-volume retailers. A recent Gallup poll commissioned by the National Association of Convenience Stores indicated that 96 percent of Americans are convenience store shoppers, and that 47 percent shop in convenience stores two or more times a week. Both statistics represent increases over the last four years, so the potential 7-Eleven customer base has actually expanded.

We believe that our customers want an everyday fair *value*, and that means a *combination* of product quality and variety, convenience, store atmosphere *and* price that they can't get elsewhere. While we have made much progress during the last year, we recognize that our stores can improve significantly in all of these areas.

Because 7-Eleven's daily customer count per store is already higher than the industry average, our best immediate opportunity is to increase the average transaction size and continue to improve our merchandise gross profit margins. We are striving for same-store sales increases in 1993 as more stores develop experience with the AIM process. However, same-store sales are not expected to climb appreciably before 1994.

One important way we plan to increase profitability over the long term is by improving our fresh fast foods, which today represent less than nine percent of our sales. Ready-to-eat food typically produces larger transactions because of associated sales, and the margins on many fast food items are higher than 7-Eleven's overall gross profit margin. However, we're just now beginning negotiations with potential suppliers that could ensure the product quality and variety our customers want, so major improvement in our national fast food program will probably not occur until 1994. Our remodeling program will also enhance 7-Eleven fast food merchandising with brighter, less cluttered stores and appealing open-front fresh food cases.

Our most important immediate task is to help our franchisees, employees and licensees better understand and apply 7-Eleven's new merchandising process to more product categories. At the same time, we must meet the significant logistical challenges of a store remodeling program that is unprecedented in scope. We will continue to look for ways to improve our organization so that we can exceed the expectations of convenience store customers, and do it more profitably than anyone else. We expect in 1993 to begin realizing the benefits of the hard work and difficult decisions made over the last two years, and we appreciate your continued interest in Southland.

Sincerely,

Clark Matthews

Clark J. Matthews II
President and Chief Executive Officer

March 12, 1993

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The franchisees, store managers and field consultants featured in this report represent the forefront of Southland's new Accelerated Inventory Management (AIM) process. Among the first to begin implementing AIM, these store operators and their staffs have committed the energy and focus to make the process work. As a result, they were rewarded in 1992 with merchandise inventories that turned about 32 percent faster than the company average and some of the best sales comparisons in their respective markets.

Without exception, the featured store managers and franchisees credit much of their success to their employees, whom they have taught to use the AIM process for item-by-item tracking, ordering and merchandising in their assigned product categories.

Southland can now focus exclusively on its 7-Eleven stores, since it has divested its non-convenience retailing businesses over the last several years. Those efforts culminated in the sale of the company's distribution and food processing business in November 1992.

In addition to 5,997 7-Eleven stores in the United States and Canada, the operations included 112 High's Dairy Stores and 58 Quik Mart and Super-7 high-volume gasoline locations open at the end of the year. Approximately half of Southland's stores are operated by franchisees, and sales from these stores are included in the company's total revenues.

SCOTT MAIN, ***FRANCHISEE***
TOM'S RIVER, NEW JERSEY

"If I didn't expect a lot of good things to happen with AIM, I wouldn't be planning to invest my money in a fourth 7-Eleven store," says 14-year franchisee Scott Main. In addition to the profit potential he anticipates from using AIM, Scott says it has also given him the system he needs to delegate ordering to his employees.

Starting on small sections of his stores in late 1991, he gradually built to the point where about 60 percent of his product mix is now managed by AIM.

Scott increased his gross profit margin about 1.5 percentage points, partly due to actions taken after a pricing survey made with his field consultant, and his stores are experiencing double-digit sales increases, which he attributes primarily to AIM.

Once he had accumulated item-by-item sales histories on several product categories, Scott found that he needed to delete many items from his stock. "We rarely took anything out of the store before AIM, but now we have a process that frees up a lot of shelf space for new products. We've learned how to really keep inventory moving, without missing sales opportunities by being out-of-stock," he explains.

"We never used to know when a new product was available; it just appeared in the order books. Now we receive a lot of information about products as soon as they're out, and we know what the customer demographic profile is for each item, so we can order correctly for each store.

"It's not an overnight process," he stresses. "You have to take it in stages. I'd say it takes a year for AIM to really become a part of your business. But I could never go back to the old way."

While convenience retailing operations accounted for $7.15 billion or 96.3 percent of Southland's net sales in 1992, 7-Eleven will be virtually the company's *only* business in 1993 — for the first time in history.

Total revenues of $7.48 billion also included other income of $51.3 million, comprised primarily of royalties from 7-Eleven area licensees and interest income. Area licensees and affiliates

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operate 6,952 stores in 18 other countries and three U.S. territories, as well as 641 stores in the United States. (See inside back cover.)

In 1992, Southland's same-store merchandise sales (sales at stores open more than one year) decreased 3.9 percent, producing negative real growth of 5.6 percent after adjusting for 7-Eleven-specific inflation of 1.9 percent. The sales decrease is partly attributable to a strategic decision to reduce discounting and price promotions, which helped increase the merchandise gross profit margin by .75 percentage point.

Southland is one of the country's largest independent gasoline retailers, at year-end selling gasoline at 2,241 locations, mostly under the "CITGO" brand name. In spite of declining consumption in the U.S., gallons sold per store increased 6.3% percent over 1991 levels, due to successful value-added promotions, the customer appeal of upgraded canopies and dispensers, and the effect of closing certain low-volume locations.

"If I didn't expect a lot of good things to happen with AIM, I wouldn't be planning to invest my money in a fourth 7-Eleven store."

Scott Main, franchisee

BIANCA HEARD, *STORE MANAGER* AND
BILL HOUSTON, *FIELD CONSULTANT*
DENVER, COLORADO

"Last year, we were practicing AIM. This year our goal is to perfect it, and that means trying a lot of new products," says Denver field consultant Bill Houston.

Bianca Heard manages a high-volume, inner-city 7-Eleven store in Bill's supervisory group of stores, and there's no doubt to anyone who comes in that she runs a tight ship. That's why the discoveries Bianca made when she first started applying AIM in her store were so surprising.

"You've been around your business for years and you think you know it, but you really don't until you have a tool like AIM to show you what's selling and what's not," she says.

The enthusiasm of Bianca and her employees for AIM helped produce a very strong sales increase in 1992. She usually tries about 75 percent of the new products that are offered each week, and is gradually stepping up the deletion of slow-moving items in her store.

Both Bill and Bianca say that AIM and every other aspect of 7-Eleven are easier to manage because of ISDP (Individual Store Development Process), a companywide business development tool launched in late 1991. As part of ISDP, the job description of the field consultant, the front-line management position over a group of 7-Eleven stores, was totally revamped to facilitate more professional, business-building relationships with store operators.

Bianca says, "Bill and I listen to each other more now, and we work toward mutual goals. In turn I quit being a taskmaster and started delegating a lot of duties, especially AIM, to my employees. You've got to empower people and just realize that sometimes mistakes are going to be made. We're all a lot more productive now."

"Last year, we were practicing AIM. This year our goal is to perfect it, and that means trying a lot of new products."

Bill Houston, field consultant

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"...it takes a year for AIM to really become a part of your business. But I could never go back to the old way."

Scott Main, franchisee

7-Eleven also benefited from more favorable retail and wholesale gasoline market conditions in 1992 as the gross profit margin increased two cents to 11.9 cents per gallon. Through centralized inventory control and pricing management, Southland has achieved continuous improvement in its gasoline operations over the last five years, interrupted only by the Gulf War's disruptive effect on market conditions in early 1991.

Southland's total gasoline gross profits increased 19.2 percent in 1992, even though gasoline was sold at about 170 fewer locations than during 1991. The total 1.38 billion gallons sold accounted for 22.5 percent of the company's convenience store sales in 1992, and a much higher percentage in the 7-Eleven locations where gasoline is sold.

KAREN HITCHCOCK, *FRANCHISEE*
LAS VEGAS, NEVADA

Karen Hitchcock's store across the street from the Las Vegas Convention Center requires heavy-duty sales forecasting and target marketing. For part of the year, it's a typical neighborhood 7-Eleven store, albeit in a city that never sleeps. During the eight-month convention season, however, Karen's customer base becomes almost humorously elastic — growing and contracting by an additional 30,000 to 100,000 people every few weeks.

To prepare, Karen gets schedules for the convention center as well as a nearby coliseum and concert hall well in advance. "With years of practice, we've learned how not to run out of anything," she says. "We know when we need to use every coffee pot, including the 100-cup reserve pot, and I work with my vendors to make sure they can meet my crazy needs — for example, doughnuts replenished as often as three times a day," she explains.

Sales forecasting enables Karen not only to stock the right quantities of products depending on the size of the conventions, but also to know what brands will be most in demand. She tracks product preferences for soda and beer for each convention, since many of the groups return every year.

Karen also prepares for conventions with special needs. For example, people at computer conventions use a *lot* of paper towels and spray cleaner for terminal screens. Karen orders enough inventory to meet the anticipated heavy demand, and then merchandises it on a convenient display to spark impulse sales.

Karen says AIM has honed her inventory management skills, especially with her grocery items. With understandable confidence, she maintains, "I was doing a good job before; now I'm doing a great job with inventory management."

"I was doing a good job before; now I'm doing a great job with inventory management."

Karen Hitchcock, franchisee

SOUTHLAND CONVENIENCE STORE SALES BY CATEGORY

Gasoline	22.5%
Tobacco Products	19.2%
Beer/Wine	10.0%
Soft Drinks (includes Slurpee®)	10.0%
Groceries	8.5%
Food Service (includes coffee)	8.4%
Non-foods	5.8%
Dairy Products	4.9%
Candy	3.8%
Baked Goods	3.4%
Customer Services (includes lottery gross profit)	1.9%
Health/Beauty Aids	1.6%
Total	100.0%

(Percentages are approximate.)

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Southland continued pruning its store base in 1992, closing or selling 358 stores due to divestitures, changing market patterns, lease expirations, relocations or poor performance, and only opening 34 new stores. Because the company is devoting its

During 1992 the company began implementing a new merchandising process called Accelerated Inventory Management or AIM. (See pages 2 and 3.) Many factors affect sales growth, but based on the success of those divisions where AIM was most fully implemented

"You've been around your business for years and you think you know it, but you really don't until you have a tool like AIM to show you what's selling and what's not."

Bianca Heard, store manager

MILTON GIBSON, *FIELD CONSULTANT* AND
JOHN GARCIA, *STORE MANAGER*
FORT WORTH, TEXAS

Veteran store manager John Garcia enthusiastically embraced AIM's deletion process for slow-moving items, removing about 800, or one-third, of the products from his store in the first eight months of applying the program. He has already introduced 600 new items, and tells his employees to try any new products that the company makes available that are suitable for his store's customers.

Aggressive and thoughtful merchandising, including a direct-mail campaign, enabled John to increase his profitability and virtually maintain his sales level in 1992 — a year his store's neighborhood was devastated by the phase-out of a nearby air force base and the loss of two air shows, layoffs at a major contractor, and road construction during the prime summer selling season.

John and his field consultant, Milton Gibson, applaud the changes Southland has made in the last two years, including the introduction of the ISDP business development tool.

Milton explains, "We've done away with a lot of obstacles, things that wasted time or were unnecessary. We used to spend most of our time just delivering and picking up paperwork, and now we have couriers to do that. Field consultants finally have the time to listen to the store managers' concerns about what's going on in the stores. The company has a completely different management style now."

John adds, "Before ISDP, my field consultant and I spent most of our time on paperwork or putting out fires. Now we sit down for two to four concentrated hours every week and figure out how to improve customer service. It's just a better way of doing business."

resources to improving the image and profitability of existing stores, it expects to have net unit decreases in the near term.

in 1992, Southland believes that the AIM process is the company's best tool for increasing sales, inventory turns and profitability. By the end of the year, all company-operated and most franchised

"The company has a completely different management style now."

Milton Gibson, field consultant

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7-Eleven stores had begun applying the AIM process on at least 25 percent of the products carried.

While AIM is geared toward immediately improving the in-store merchandising of all 7-Eleven stores, the company has also begun the rollout

"I liked ISDP from the start because it focused on my store."
Paul Ung, franchisee

MARK LOFFER, *FIELD CONSULTANT* AND PAUL UNG, *FRANCHISEE* TUKWILA, WASHINGTON

Paul Ung has only been a franchisee since late 1991, but he has an experienced 7-Eleven perspective — having spent the previous 10 years as a manager for a company-operated store in Washington, D.C. He and his field consultant, Mark Loffer, agree that the company's new business development process (ISDP) was a much-needed improvement.

Paul notes, "I liked ISDP from the start because it focused on my store. We needed to learn to communicate better in both directions. That's what I pay for as a franchisee — consultation. Sometimes Mark and I disagree about something, but we're OK as long as we agree to disagree."

"When I was a store manager, before ISDP, my field consultant would come into the store maybe three times a week, pick up some paperwork, check on things for half an hour, and leave. Now Mark and I draw up agendas in advance of our meetings, then we spend three to four hours working on this week's issues and setting priorities and goals for the coming week," Paul continues.

Paul uses ISDP tools with his own employees, holding weekly individual and monthly group meetings. "I get them involved as much as I can, so they really know how to take care of things," he says.

Each of Paul's employees is assigned a certain section of the store to count, order and merchandise according to the AIM process. Meeting their own challenges and weekly goals has made the employees' jobs more interesting and reduced turnover. Paul emphasizes, "They say 'now, this is our store, too.' We all work as a team. Even if I weren't here, the store would still run."

of a four-year remodeling program that will transform the appearance of its store base. The company has budgeted approximately $200 million for 1993 capital expenditures, about the same amount spent in the last three years combined. The majority of the 1993 capital expenditure budget will be used to remodel the interiors and exteriors of approximately 1,300 stores in 11 markets.

After two decades of operating its own distribution centers, in late 1992 Southland signed a service agreement with McLane Company, Inc., the country's largest convenience store distributor. McLane is now offering coast-to-coast distribution services to

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all 7-Eleven stores from a single source for the first time in history. Although any major transition such as this involves significant operating challenges for both parties, the new arrangement with McLane is a key to Southland's long-term strategy to respond more quickly and offer better value to its customers. McLane will provide 7-Eleven greater buying efficiency and more supply points located closer to 7-Eleven stores, which will facilitate more frequent deliveries.

"We're going in the right direction, even if it is a lot of work. AIM and ISDP have breathed new life into us. For those who want to improve sales, we now have the tools to do it."

Patty Miller, franchisee

PATTY AND GLENN MILLER, *FRANCHISEES*
CENTER LINE, MICHIGAN

"It's amazing to look back on how we used to manage our inventory. We never changed what we had on our shelves or how they were merchandised, and it took a long time to get new products. It's getting easier now that the company has removed some layers, and I think being supplied by McLane is going to improve things," says Patty Miller, who franchises two stores north of Detroit with her husband Glenn.

Patty says her enthusiasm has been restored after 13 years of franchising. "Things had gotten boring. Now we have real eye-openers every week because of the information we're getting from AIM. We've got things to think about that get us more involved in the business, and we've got data to use to help us make decisions and track results," she explains.

Although the Millers' overall inventories decreased substantially after following AIM for several months, Patty emphasizes that the process is "more than cutting inventory, it's *managing* inventory so that customers always find what they want." She was surprised to find out how many sales she was missing on a certain brand of cigarettes, simply because the order quantity had never been increased to match the demand. Using her new sales data, she also halved the pet food section in one store without affecting her sales.

Patty saw another benefit — valuable input from her employees — immediately after starting AIM. "As soon as I explained the new-item process, it was like someone turned on a light bulb. My employees started telling me about all the things that customers asked for that we didn't stock; it hadn't occurred to them that I'd be interested," Patty says.

"We're going in the right direction, even if it is a lot of work. AIM and ISDP have breathed new life into us. For those who want to improve their sales, we now have the tools to do it."

SOUTHLAND'S BUSINESS CONCEPT

"To serve the customer through 7-Eleven stores that achieve a sustainable competitive advantage through superior merchandising... a proprietary process that gives us item-by-item control at each store, providing convenience-oriented customers with what they want...

SPEED... A fast transaction
QUALITY... on those fresh, high-quality products
SELECTION... that they want and need
PRICE... at a fair price
ENVIRONMENT... in a clean, safe, friendly store.

This can only be accomplished through a productive, motivated and efficient organization of franchisees, licensees and employees and with the support of our suppliers and manufacturers."

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(Dollars in Millions, Except Per-Share Data)	Years Ended December 31 1992	1991	1990	1989	1988
Net sales	$ 7,425.8	$ 8,009.5	$ 8,347.7	$ 8,274.9	$ 7,950.3
Other income	51.3	66.5	62.4	77.0	40.2
Total revenues	7,477.1	8,076.0	8,410.1	8,351.9	7,990.5
LIFO charge (credit)	1.5	(7.2)	27.9	2.8	19.1
Depreciation and amortization	180.3	200.1	227.6	276.7	294.7
Interest expense	123.6[a]	189.3[a]	459.5	572.2	560.3
Loss from continuing operations before income taxes	(119.9)[b]	(66.3)	(430.0)[d]	(1,332.3)[f]	(397.1)
Income taxes (benefit)	11.5	8.0	(128.5)	(12.0)	(111.9)
Loss from continuing operations	(131.4)	(74.3)	(301.5)	(1,320.3)	(285.2)
Loss before extraordinary items and cumulative effect of accounting change	(131.4)	(74.3)	(301.5)	(1,250.9)[g]	(216.2)[g]
Net earnings (loss)	(131.4)	82.5[c]	(276.6)[e]	(1,306.9)[h]	(216.2)
Earnings (loss) per common share (primary and fully diluted):					
From continuing operations:	(0.32)	(0.22)	(15.14)	(65.41)	(15.63)
Before extraordinary items and cumulative effect of accounting change:	(0.32)	(0.22)	(15.14)	(62.02)	(12.19)
Net earnings (loss) applicable to common shares:	(0.32)	0.24	(13.93)	(64.76)	(12.19)
Total assets	2,044.8	2,612.4	2,813.6	3,445.8	4,865.0
Long-term debt, including current portion	2,560.4[a]	3,041.8[a]	3,705.2	4,149.5	4,314.8
Redeemable preferred stock	—	—	148.5	139.7	118.8

(a) The Restructured Debt Securities are accounted for in accordance with SFAS No. 15 as explained in Note 9 to Consolidated Financial Statements.

(b) Loss from continuing operations before income taxes includes a $45,000,000 loss on the sale and closing of the distribution and food centers as explained in Note 6 to Consolidated Financial Statements.

(c) Net earnings include an extraordinary gain on debt restructuring of $156,824,000 as explained in Note 2 to Consolidated Financial Statements.

(d) Loss from continuing operations before income taxes reflects the loss on Cityplace assets sold of $41,000,000 as explained in Note 6 to Consolidated Financial Statements.

(e) Net loss includes an extraordinary tax benefit from utilization of net operating loss carryforwards of $52,040,000 and a charge for the cumulative effect of an accounting change for postretirement medical benefits expense of $27,163,000 as explained in Notes 16 and 14 to Consolidated Financial Statements, respectively.

(f) Loss from continuing operations before income taxes reflects the write-off of $946,974,000 of excess of cost over fair value of net assets acquired.

(g) Loss before extraordinary items and cumulative effect of accounting change include earnings from a discontinued operation (Citgo) of $69,410,000 and $69,001,000 for 1989 and 1988, respectively.

(h) Net loss includes an extraordinary charge of $56,047,000 resulting from a debt exchange.

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Liquidity and Capital Resources

On February 21, 1991, four months after filing a voluntary petition under Chapter 11 of the U.S. Bankruptcy Code, the Company's plan of reorganization (the "Restructuring") was confirmed by the U.S. Bankruptcy Court for the Northern District of Texas. The Restructuring included the exchange of the Company's $1.5 billion of public debt securities (the "Old Debt Securities") and 15% Cumulative Exchangeable Preferred Stock (the "Redeemable Preferred Stock") for new debt securities (the "Restructured Debt Securities"), common stock (the "Common Stock"), and/or cash and warrants to purchase shares of Common Stock, at a price of $1.75 per share, from certain of the existing shareholders of the Company, including the founding Thompson family (the "Thompson Warrants").

On March 5, 1991, the Company consummated the Restructuring and completed its bankruptcy reorganization with the closing of a Stock Purchase Agreement (the "Stock Purchase Agreement") with IYG Holding Company (the "Purchaser"), which is a jointly owned subsidiary of Ito-Yokado Co., Ltd., and Seven-Eleven Japan Co., Ltd. Under the terms of the Stock Purchase Agreement, the Purchaser acquired approximately 70% of the Company's Common Stock for $430 million in cash. Following private transactions, the Purchaser now holds approximately 64% of the shares currently outstanding.

Pursuant to the Restructuring, and subsequent to the pro rata allocation of Thompson warrants, holders of the Company's old securities were entitled to exchange, until March 5, 1993, their old securities for new debt, common stock, and/or cash and the Thompson Warrants as follows: all holders of each $1,000 principal amount of the Company's 13 1/2% Senior Extendible Reset Notes due 1995 were entitled to receive $475 principal amount of 12% Senior Notes due 1996 (the "New Senior Notes"), 86.5 shares of the Company's Common Stock, $57 in cash and one Thompson Warrant; all holders of each $1,000 principal amount of its 15 3/4% Senior Subordinated Notes due 1997 were entitled to receive $650 principal amount of 5% First Priority Senior Subordinated Debentures due 2003 (the "New First Priority Debentures"), 40.5 shares of Common Stock and 8.2 Thompson Warrants; all holders of each $1,000 principal amount of its 16 1/2% Senior Subordinated Discount Notes due 1997 were entitled to receive $555 principal amount of New First Priority Debentures, 35 shares of Common Stock and 7.2 Thompson Warrants; 82.5% of the holders of each $1,000 principal amount of its 16 3/4% Subordinated Debentures due 2002 were entitled to receive $500 principal amount of 4.5% Second Priority Senior Subordinated Debentures (Series A) due 2004, 28 shares of Common Stock and 6 Thompson Warrants, while the remaining 17.5% of the holders have elected to receive $250 principal amount of 12% Second Priority Senior Subordinated Debentures (Series C) due 2009 and 28 shares of Common Stock; all holders of each $1,000 principal amount of its 18% Junior Subordinated Discount Debentures due 2007 were entitled to receive $257 principal amount of 4% Second Priority Senior Subordinated Debentures (Series B) due 2004, 11 shares of Common Stock and 6 Thompson Warrants; and holders of each share of its Redeemable Preferred Stock were entitled to receive one share of Common Stock and .073 Thompson Warrants.

In December 1987, the Company issued Warrants (the "Old Warrants") as part of the securities issued in the Company's leveraged buyout. The Old Warrants expired in December 1992 without becoming exercisable and were independently valued as worthless. Therefore, all outstanding Old Warrants were cancelled as of March 15, 1993.

In September 1992, the Company began issuing commercial paper in a program that can raise up to $400 million based upon the Company's needs. The commercial paper is unconditionally guaranteed by Ito-Yokado Co., Ltd., and has the highest investment grade ratings. As part of the new financing, the Company amended its senior bank credit agreement (the "Credit Agreement") to extend its revolving credit facility ("Revolver") from December 31, 1992, to December 31, 1995, and to modify certain financial covenants for the Revolver extension period. Upon approval of the amendment, the Company prepaid $350 million of the senior term loan (the "Term Loan"). In October, the Company negotiated a subsequent amendment to the Credit Agreement that permitted it to sell certain of the Company's distribution and food center assets to McLane Company, Inc.,

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("McLane"). After closing under the purchase and sale agreement on November 30, 1992, the Company paid $110 million of sales proceeds to its senior lenders, leaving the balance of the Term Loan at $238 million with remaining amortizations of $50 million, $75 million and $113 million in 1993, 1994 and 1995, respectively. In the first quarter of 1993, half of the 1993 amount was prepaid. The bank debt, which was originally $2.5 billion, will be retired by September 30, 1995.

In July 1992, the Company redeemed the 12% Canadian Notes, which had a remaining principal balance on June 30, 1992, of approximately U.S. $33 million.

Cash Flows from Operating Activities

During the twelve months ended December 31, 1992, net cash provided by operating activities was $178.0 million. This amount included increases in cash flows from a $12.3 million reduction in inventories due to the Company's ongoing effort to improve its inventory management, and $8.4 million of net income tax refunds for prior years.

Cash Flows from Investing Activities

During the twelve months ended December 31, 1992, cash used in investing activities consisted primarily of payments of $88.6 million for property, plant and equipment, the majority of which was used for upgrading stores, enhancing gasoline facilities and providing maintenance to certain existing stores. In 1993, the Credit Agreement permits the Company to incur capital expenditures of up to $174 million (plus up to $75 million of amounts unspent in 1992). The Company expects to spend up to $200 million in 1993 to extensively remodel approximately 1,300 of its existing stores, to provide required maintenance to other stores, and for maintenance of underground storage tanks.

The Company continues to anticipate that it may have increased maintenance expenditures in the future in connection with environmental requirements related to upkeep of its gasoline storage tanks at store locations. The Company currently estimates that it will be required to spend approximately $40 million on capital improvements over the next five years in order to comply with governmental requirements affecting gasoline storage tanks. These expenditures are higher than previously expected, because the Company has chosen to make certain expenditures in conjunction with its extensive store remodeling program that otherwise would not have been required to be made until 1998. Approximately $23 million of this total will be spent in 1993.

The Company expects that it will be required to spend between $45 and $60 million during the next three years to undertake corrective action for known releases of regulated substances at its existing and previously operated gasoline sites. The Company also expects that these future remediation costs will be more than completely offset by state reimbursements of such future costs, as well as of unreimbursed remediation costs incurred prior to December 31, 1992. The Company has, therefore, not accrued any expense for expected future remediation costs. The estimated future remediation expenses and related state reimbursement amounts could change as governmental requirements and state reimbursement programs are more fully defined, or if additional releases are discovered. Based on the Company's experience, it expects to receive state reimbursement funds within one to two years after incurring eligible remediation expenses, assuming that the states have developed the procedures for reimbursement.

On November 30, 1992, McLane acquired certain of the Company's distribution and food center assets including the San Bernardino, California, distribution center; the Fredericksburg, Virginia, distribution and food center; and the food centers in Salt Lake City, Utah, and St. Louis, Missouri. In addition, Southland ceased operations at its distribution and food centers in Orlando, Florida, and Tyler, Texas, in December 1992, and will do so in Champaign, Illinois, in April 1993. As a result of this sale and the related plant closings, the Company recognized a loss of $45 million. Through December 31, 1992, the Company has received $141.8 million in gross proceeds. Additional proceeds of approximately $50 million will be received in 1993 from the collection of certain of the Company's accounts receivable and the sale of remaining inventories. During the last four months of 1992, $54.0 million of cash was used by these distribution and food center operations; approximately $35 million to reduce accounts payable and make severance payments and approximately $19 million to purchase inventories that were primarily sold to McLane at the closing.

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In connection with the sale of assets to McLane, the Company entered into a long-term service agreement that it believes will benefit the Company and 7-Eleven franchisees by making available nationwide distribution service from a single source to the nearly 5,700 7-Eleven and other Southland convenience stores in the United States. The Company expects the service agreement to lower 7-Eleven wholesale merchandise costs. In addition, because of McLane's expanded network, more distribution centers will be located closer to 7-Eleven stores, which will facilitate more frequent deliveries of merchandise at competitive prices.

The Company is continuing its efforts to sell approximately 180 stores in various markets.

Cash Flows from Financing Activities

During the twelve months ended December 31, 1992, the Company repaid $530.5 million on certain secured indebtedness, primarily $492 million for reduction of the Term Loan. In addition, the Company paid $33.5 million to redeem the 12% Canadian Notes, and $65.3 million in interest payments related to the Restructured Debt Securities that were charged against their recorded amounts as required by SFAS No. 15, rather than being recorded as interest expense. As of December 31, 1992, there were no borrowings under the Revolver, but $140.1 million in letters of credit were outstanding, and $221.9 million of commercial paper was outstanding. In the future, the Company expects to continue to use the Revolver primarily for letters of credit, and the $400 million commercial paper facility for liquidity purposes. Under the Credit Agreement, the Company's cash availability from the Revolver is limited to $25 million until $375 million of commercial paper is outstanding, and thereafter to $150 million.

Results of Operations —
Twelve Months Ended December 31, 1992

The Company recorded net sales of $7.43 billion in the twelve months ended December 31, 1992, compared to net sales of $8.01 billion for the same period last year. The decline is primarily due to an average of about 260 fewer convenience stores, lower outside sales by the distribution and food centers (which were included for only eight months in 1992), and lower same-store (stores open more than one year) merchandise sales. Convenience store sales accounted for 96.3% of net sales in 1992. Same-store merchandise sales decreased 3.9% in 1992 while 7-Eleven experienced an annualized inflation rate of 1.9%, resulting in negative real growth of 5.6%. 7-Eleven has experienced negative real growth in merchandise sales since early 1989 because of competitive pressures and the recession, and more recently due to a strategic decision to reduce discounting and promotional activities in favor of an "everyday fair price" strategy. Gasoline sales per store increased 6.5% in 1992, due to upgraded gasoline facilities, the continued improvement in gasoline inventory and price management, and the effect of closing certain low-volume locations.

Other income of $51.3 million in 1992 consisted primarily of royalties from area licensees, principally Seven-Eleven Japan, and interest income that was partially offset by a loss of $17.0 million on the divestiture of 45 stores in 1992 and the planned divestiture of certain stores in 1993.

The Company's consolidated gross margin (gross profit divided by sales) was 21.6%. The convenience stores' merchandise gross margin increased 0.75 percentage points in 1992 when compared to 1991, primarily due to a reduction in discounting and promotional activities, a key part of the Company's new merchandising strategy. For the year, merchandise gross profits per store were down slightly from 1991 due to the reduction in per-store merchandise sales, which offset the increased margins. Gross profit on retail gasoline sales was 11.9 cents per gallon in 1992, an increase of 2.0 cents when compared to last year. Per-store gallonage increased 6.3% over 1991 levels, due to the effect of closing certain low-volume locations, capital expenditure programs begun last year and favorable market conditions. (Except where noted, all per-store numbers above refer to an average of all stores rather than only stores open a year or more.)

Selling, general and administrative expenses ("SG&A") increased $7.7 million in 1992. The ratio of SG&A expenses to sales was 21.5% for the year, an increase of 1.66 percentage points compared to 1991. The increase primarily reflects lower sales and higher expenses associated with implementing the Company's business plan, including a $17.5 million expense for severance and related costs of a reduction in force, and a $17.5 million expense for store closings which occurred in 1992 and are planned for 1993. A cost-cutting program, which began in the third quarter and is designed to control future SG&A expense, is part of an ongoing company-wide effort to centralize and consolidate various stores' support functions, improve communications and improve

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the Company's ability to respond faster and more creatively to rapidly changing customer needs and preferences. The reduction in force resulted in approximately $9.1 million of savings from reduced salaries and wages in 1992, and the Company anticipates that there will be 1993 cost savings of approximately $50 million.

In 1991, the Company began an intensive business review to identify, test and develop strategies and programs designed to improve sales and profits and provide 7-Eleven stores with a competitive advantage over the longer term. The Company currently is adopting a more customer-driven approach to merchandising, intended to greatly expand and improve the quality and variety of 7-Eleven's product selection by phasing out slow-selling items and aggressively introducing high-turnover items and new products in the early stages of their life cycle. The new merchandising process was implemented, to varying extents, in most 7-Eleven stores by December 31, 1992, and it is the Company's goal to implement it more extensively in all stores in 1993. In 1992, this new process has improved sales and profits in those stores that are applying it to a significant number of major product categories. Southland is also implementing a new retail pricing strategy to reduce certain prices, minimize discounting and promotions and instead charge an "everyday fair price," which is somewhat higher than supermarket prices, to reflect the value of convenience. As anticipated, this pricing strategy, together with fewer and shorter promotions, is initially having a negative impact on merchandise sales, but is enhancing margins and is expected to improve them further over the long term.

The upfront cost of introducing new programs, combined with soft economic conditions, caused the Company's 1992 operating earnings for the year to decline compared to those experienced in 1991. However, the Company experienced improved operating results in the fourth quarter compared to the same period in 1991. The Company expects that its business plan, including the new merchandising programs, increased capital spending, closure of unprofitable stores, reduced interest expense, the sale and closure of the distribution and food centers, and the reduction in force will improve its ability to compete more effectively, and the Company believes this will result in net earnings in 1993.

The Company's total interest expense decreased $65.6 million in 1992 compared to 1991, primarily due to declining interest rates on the Term Loan and lower Term Loan balances. In 1992, the weighted average interest rate of the Company's floating rate debt was 6.56%. Going forward, the Company expects its interest expense to decline further due to lower average debt balances and the use of commercial paper at favorable rates. Given the Company's high percentage of fixed rate debt, in December 1991 the banks eliminated the hedging requirement from the Credit Agreement, and the Company currently has no interest rate hedges outstanding.

The business plan described above resulted in nonrecurring charges which obscured the gradually improving operating performance. The Company recorded a net loss of $131.4 million for the year ended December 31, 1992, which includes a $17.5 million provision for severance and related costs, as well as $34.5 million of charges for store divestitures and closings, and a $45 million loss on the sale and closing of the distribution and food centers. This compared to net earnings of $82.5 million for the same period last year, which included an extraordinary gain on the restructuring of $156.8 million. Losses per common share for 1992, both primary and fully diluted, were $.32.

During February 1992, the Financial Accounting Standards Board issued SFAS No. 109, "Accounting for Income Taxes," which supersedes SFAS No. 96. The Company will adopt this statement as of January 1, 1993. The Company estimates that there will be no cumulative effect on earnings upon adoption of SFAS No. 109 because it will record a net deferred tax asset, which will be fully reserved.

In November 1992, the Financial Accounting Standards Board issued SFAS No. 112, "Employers' Accounting for Postemployment Benefits." The statement requires recognition of an obligation for all benefits provided by an employer to former or inactive employees after employment but before retirement (postemployment benefits) and must be adopted no later than 1994. The Company has not completed its review of the requirements of the statement and therefore has not determined the impact on earnings in the year of adoption. The Company has not yet decided when it will adopt the statement.

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Results of Operations —
Twelve Months Ended December 31, 1991

The Company recorded net sales of $8.0 billion for the twelve months ended December 31, 1991, versus $8.3 billion for the same period in 1990. The decline was primarily due to fewer convenience stores, lower retail gasoline prices and the phasing out of outside foodservice business at the distribution centers. Convenience store sales of $7.5 billion accounted for 94% of net sales. Same-store merchandise sales increased .26% in 1991 while 7-Eleven experienced an annualized inflation rate of 2.8% for the same period, resulting in negative real growth of 2.5%. Gasoline sales per store decreased 3.2% due primarily to lower average retail prices.

Other income of $66.5 million in 1991 consisted primarily of royalties from area licensees and interest income.

The Company's consolidated gross margin was 20.68% in 1991. The convenience stores' merchandise gross margin decreased 0.49 percentage points due to the recession and competitive pressures. Gross profit on retail gasoline sales decreased to 9.9 cents per gallon in 1991 from 11.6 cents in 1990 due primarily to unusually aggressive pricing by integrated oil companies. Gallonage on a per-store basis remained virtually flat, despite an approximate 4% decline in overall U.S. consumption, mostly as a result of successful marketing efforts.

Selling, general and administrative expenses decreased $78.8 million in 1991. The decline for the year was primarily attributed to $20.2 million less in Restructuring expenses and approximately $23 million in ongoing savings associated with certain cost reduction measures. As a result, the ratio of selling, general and administrative expenses to sales was 19.8%, a decrease of .14 percentage points from the same period in 1990.

In 1991, the Company began some important marketing tests and implementation of inventory management processes aimed at emphasizing item-by-item tracking of merchandise at each store to eliminate slow-moving merchandise and introduce new, faster-moving items. Some of these plans, like a program to enhance communications between the Company's field staff, franchisees and store managers based on individual store development plans, were expected to improve customer service and increase merchandise sales. However, they were also expected to have an initial negative impact on earnings during their start-up in 1992. In addition, the Company's labor costs were expected to rise in the future due to wage increases and compliance with any local legislation that may require additional personnel to operate the stores.

Although the Company's merchandise sales increased on a per-store basis during 1991, these increases did not compensate for the decrease in merchandise margins that resulted from the effects of the recession and competitive pressures. As a result of the then-current economic outlook, intense competition, significantly lower-than-anticipated capital expenditures in 1991 and implementation of new programs, the Company expected its operating results to decline further in 1992.

The Company's total interest expense decreased $270.2 million during 1991, which included $231.3 million in interest on the Old Debt Securities, primarily due to the effects of the Restructuring. The Company stopped accruing interest on the Old Debt Securities at the time it filed bankruptcy. In addition, as required by SFAS No. 15 the related interest payments on the New Debt Securities were not being charged to interest expense, but rather were charged against their recorded amounts. Additional factors included lower Term Loan balances, declining interest rates on the Term Loan and the absence of borrowings under the Credit Agreement's revolving credit facility after consummation of the Restructuring. As a result of the above factors, the Company's reported interest expense was expected to be significantly reduced in the future.

At December 31, 1991, approximately 53% of the Company's bank term debt was hedged against future interest rate increases. In 1991, the weighted average interest rate of the Company's Term Loan indebtedness under the Credit Agreement, including the cost of hedging and interest swaps, was 11.5%. The net cost of hedging was $8.4 million higher than interest expense would have been without hedging.

In accordance with SFAS No. 15, the Company recognized a gain on the Restructuring of $156.8 million for the twelve months ended December 31, 1991. In addition, shareholders' equity increased by $127.8 million as a result of the exchange of Redeemable Preferred Stock for Common Stock associated with the Restructuring.

As a result of the factors described above, and a foreign tax expense of $8.0 million, the Company's net earnings for the year ended December 31, 1991, were $82.5 million.

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Results of Operations —
Twelve Months Ended December 31, 1990

The Company recorded net sales of $8.3 billion for the twelve months ended December 31, 1990. Convenience store sales of $7.7 billion accounted for 92% of net sales. Same-store merchandise sales increased .83% in 1990 while 7-Eleven experienced an annualized inflation rate of 3.8% for the same period, resulting in negative real growth of 2.8%. Gasoline sales per store increased 17.3% due to higher average retail prices and a continuing shift in the sales mix to higher grades of gasoline.

Other income of $62.4 million in 1990 consisted primarily of royalties from area licensees and interest income.

The Company's consolidated gross margin (gross profit divided by sales) was 20.2% in 1990. The convenience stores' merchandise gross margin increased 0.59 percentage points primarily due to continued promotional emphasis on higher-margin products and pricing strategies that better reflected market opportunities. Gross profit on retail gasoline sales was 11.6 cents per gallon in 1990, compared to 11.5 cents in 1989.

Selling, general and administrative expenses increased $57.3 million in 1990. The Company recognized $31 million in expenses related to fees for the Restructuring, other restructuring alternatives that were considered by the Company, and bankruptcy-related fees. In addition, franchisees' gross profit increased by $20 million. Franchisees' gross profit is the expense associated with the franchisees' share of the gross profit generated by franchised stores. As a result, the ratio of selling, general and administrative expenses to sales was 19.94%, an increase of .52 percentage points from the same period in 1989.

The Company's total interest expense decreased $112.7 million during 1990 as compared with 1989 primarily due to lower debt balances under the bank Term Loans and the reduced borrowings under the revolving credit facility under the Credit Agreement. In addition, the Company did not make interest payments on the Old Debt Securities on June 15 and December 15, 1990; however, the Company continued to accrue for such interest through the date of the bankruptcy filing but stopped such accruals at that time. The Company would otherwise have recognized approximately $55 million of additional interest expense in the fourth quarter. Interest on the New Debt Securities, pursuant to the terms of the plan of reorganization, however, began to accrue as of June 15, 1990, at the new interest rates, and was paid on June 15, 1991.

At December 31, 1990, approximately 73% of the Company's bank term debt was hedged against future interest rate increases. In 1990, the weighted average interest rate of the Company's Term Loan indebtedness under the Credit Agreement, including the cost of hedging and interest swaps, was 11.7%. The net cost of hedging was $5.0 million higher than interest expense would have been without hedging.

In 1990, the Company recorded a tax benefit of $128.5 million related to losses from continuing operations and an extraordinary item of $52.0 million representing the tax benefit from the utilization of net operating loss carryforwards. These items offset most of the taxable gain on the sale of Citgo.

In 1990, the Company adopted SFAS No. 106, "Employers' Accounting for Postretirement Benefits other than Pensions." The cumulative effect of this change for years prior to 1990 was a $27.2 million reduction in earnings.

As a result of the factors described above, the Company's net loss was $276.6 million in 1990.

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(Dollars in Thousands, Except Per-Share Data)	December 31 1992	1991
ASSETS		
Current assets:		
Cash and cash equivalents	$ 13,954	$ 238,561
Accounts and notes receivable	131,350	125,631
Inventories	125,710	227,215
Deposits and prepaid expenses	45,882	48,582
Assets held for sale	34,309	—
Total current assets	351,205	639,989
Property, plant and equipment	1,356,163	1,592,266
Other assets	337,449	380,184
	$ 2,044,817	$ 2,612,439
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable and accrued expenses	$ 540,615	$ 601,991
Commercial paper	71,866	—
Long-term debt due within one year	152,515	168,246
Total current liabilities	764,996	770,237
Deferred credits and other liabilities	190,652	152,746
Long-term debt	2,407,928	2,873,603
Redeemable common stock purchase warrants	—	26,136
Commitments and contingencies		
Shareholders' equity (deficit):		
Common stock, $.0001 par value; 1,000,000,000 shares authorized; 410,022,481 shares issued and outstanding	41	41
Additional capital	625,724	599,588
Accumulated deficit	(1,944,524)	(1,809,912)
Total shareholders' equity (deficit)	(1,318,759)	(1,210,283)
	$ 2,044,817	$ 2,612,439

See notes to consolidated financial statements.

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(Dollars in Thousands, Except Per-Share Data)	YEARS ENDED DECEMBER 31 1992	1991	1990
Revenues:			
Net sales (including $986,962, $954,027 and $876,259 in excise taxes)	$ 7,425,844	$ 8,009,507	$ 8,347,681
Other income	51,260	66,505	62,375
	7,477,104	8,076,012	8,410,056
Cost of goods sold and expenses:			
Cost of goods sold	5,820,817	6,352,855	6,661,273
Selling, general and administrative expenses	1,593,489	1,585,804	1,664,586
Loss on sale and closing of distribution and food centers	45,000	—	—
Loss on Cityplace assets sold	—	—	41,000
Interest expense	123,647	189,290	459,500
Contributions to Employees' Savings and Profit Sharing Plan	14,100	14,411	13,653
	7,597,053	8,142,360	8,840,012
Loss before income taxes (benefit), extraordinary items and cumulative effect of accounting change	(119,949)	(66,348)	(429,956)
Income taxes (benefit)	11,500	8,000	(128,459)
Loss before extraordinary items and cumulative effect of accounting change	(131,449)	(74,348)	(301,497)
Extraordinary items:			
Gain on debt restructuring	—	156,824	—
Tax benefit from utilization of net operating loss carryforwards	—	—	52,040
Total extraordinary items	—	156,824	52,040
Cumulative effect of accounting change for postretirement medical benefits	—	—	(27,163)
Net earnings (loss)	(131,449)	82,476	(276,620)
Accretion to redemption value of redeemable preferred stock	—	—	(7,744)
Redeemable preferred stock dividends	—	—	(1,011)
Net earnings (loss) applicable to common shares	$ (131,449)	$ 82,476	$ (285,375)
Earnings (loss) per common share (primary and fully diluted):			
Before extraordinary items and cumulative effect of accounting change	$ (.32)	$ (.22)	$ (15.14)
Extraordinary items	—	.46	2.54
Cumulative effect of accounting change	—	—	(1.33)
Net earnings (loss)	$ (.32)	$ .24	$ (13.93)

See notes to consolidated financial statements.

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(Dollars in Thousands, Except Share Amounts)	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL CAPITAL	ACCUMULATED DEFICIT	TOTAL SHAREHOLDERS' EQUITY(DEFICIT)
Balance, January 1, 1990	20,504,177	$ 2	$ 20,366	$ (1,736,179)	$ (1,715,811)
Net loss	—	—	—	(276,620)	(276,620)
Dividends on redeemable preferred stock	—	—	—	(1,011)	(1,011)
Accretion to redemption value of redeemable preferred stock	—	—	—	(7,744)	(7,744)
Cancellation of grant stock	(23,333)	—	(2)	—	(2)
Foreign currency translation adjustments	—	—	—	2,628	2,628
Balance, December 31, 1990	20,480,844	2	20,364	(2,018,926)	(1,998,560)
Net earnings	—	—	—	82,476	82,476
Shares issued related to Restructuring	389,541,637	39	584,474	—	584,513
Costs associated with issuance of common stock	—	—	(5,250)	—	(5,250)
Cancellation of redeemable preferred stock in Restructuring	—	—	—	127,788	127,788
Foreign currency translation adjustments	—	—	—	(1,250)	(1,250)
Balance, December 31, 1991	410,022,481	41	599,588	(1,809,912)	(1,210,283)
Net loss	—	—	—	(131,449)	(131,449)
Adjustment for redeemable common stock purchase warrants	—	—	26,136	—	26,136
Foreign currency translation adjustments	—	—	—	(3,163)	(3,163)
Balance, December 31, 1992	410,022,481	$ 41	$ 625,724	$ (1,944,524)	$ (1,318,759)

See notes to consolidated financial statements.

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(Dollars in Thousands)	YEARS ENDED DECEMBER 31 1992	1991	1990
Cash flows from operating activities:			
Loss before extraordinary items and cumulative effect of accounting change	$ (131,449)	$ (74,348)	$ (301,497)
Adjustments to reconcile loss before extraordinary items and cumulative effect of accounting change to net cash provided by (used in) operating activities:			
Depreciation and amortization of property, plant and equipment	160,502	179,855	206,995
Other amortization	19,778	20,289	20,578
Noncash interest expense	12,429	17,508	152,490
Accrued interest not paid due to the Restructuring	—	—	113,029
Other noncash expense	22,375	12,608	6,610
Net loss on retirement of property, plant and equipment	28,563	15,304	4,753
Loss on sale and closing of distribution and food centers	45,000	—	—
Loss on Cityplace assets sold	—	—	41,000
Decrease in accounts and notes receivable	5,190	35,112	28,791
Decrease (increase) in inventories	12,252	74,541	(25,644)
Decrease (increase) in deposits and prepaid expenses	8,564	(32,449)	(40,326)
Decrease in other assets	2,869	2,310	1,837
Decrease in accounts payable and other liabilities	(8,102)	(96,796)	(213,569)
Net cash provided by (used in) operating activities	177,971	153,934	(4,953)
Cash flows from investing activities:			
Payments for purchase of property, plant and equipment	(88,575)	(69,873)	(39,624)
Proceeds from sale of property, plant and equipment	15,827	16,015	48,567
Net currency exchange principal transactions	(6,635)	(4,353)	(3,688)
Payments received on notes	1,317	1,174	9,331
Net cash received from (paid for) other investments	822	(1,290)	(5,472)
Cash utilized by distribution and food center assets	(54,020)	—	—
Proceeds from sale of distribution and food center assets	141,793	—	—
Proceeds from sale of Cityplace assets	—	—	24,000
Cash generated from Citgo, net of tax	—	—	1,649
Proceeds from sale of equity interest in Citgo	—	—	661,500
Net cash provided by (used in) investing activities	10,529	(58,327)	696,263
Cash flows from financing activities:			
Proceeds from commercial paper and revolving credit facilities	2,007,239	478,955	3,139,912
Payments under commercial paper and revolving credit facilities	(1,785,717)	(546,070)	(3,286,527)
Proceeds from issuance of long-term debt	—	—	25,000
Principal payments under long-term debt agreements	(629,300)	(328,236)	(456,646)
Proceeds from issuance of stock	—	430,011	—
Debt issuance costs	(5,329)	—	(12,800)
Net cash (used in) provided by financing activities	(413,107)	34,660	(591,061)
Net (decrease) increase in cash and cash equivalents	(224,607)	130,267	100,249
Cash and cash equivalents at beginning of year	238,561	108,294	8,045
Cash and cash equivalents at end of year	$ 13,954	$ 238,561	$ 108,294
Related disclosures for cash flow reporting:			
Interest paid, excluding SFAS15 Interest	$ (116,931)	$ (171,048)	$ (197,192)
Net income taxes refunded (paid)	$ 8,368	$ (20,350)	$ 24,847

See notes to consolidated financial statements.

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YEARS ENDED DECEMBER 31, 1992, 1991 AND 1990

1. Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of The Southland Corporation and its subsidiaries (referred to as the Company). Intercompany transactions and account balances are eliminated. Certain prior year amounts have been reclassified to conform to current year presentation.

Revenues

Net sales, which include excise taxes, are comprised of sales of products and services, including net sales by stores operated by franchisees of $2,931,494,000, $3,065,542,000 and $3,065,776,000 from 3,011, 3,045 and 3,058 stores for the years ended December 31, 1992, 1991 and 1990, respectively. Under the present franchise agreements, initial franchise fees are recognized in income currently and are generally calculated based upon gross profit experience for the store or market area, to cover certain costs including training, an allowance for travel, meals and lodging for the trainees and other costs relating to the franchising of the store. Continuing franchise fees, which generally range from 50% to 58% of the gross profit of the store, are charged to the franchisee for the license to use the 7-Eleven operating system and trademarks, for the lease and use of the store premises and equipment and for continuing services provided by the Company. These services include merchandising, advertising, recordkeeping, store audits, contractual indemnification, business counseling services, training seminars and preparation of financial statements.

Sales by stores operated under domestic and foreign area license agreements are not included in consolidated revenues. All fees or royalties arising from such agreements are included in other income. Initial fees, which have been immaterial, are recognized when the services required under the agreements are performed.

Other income is primarily comprised of area license royalties, interest income, and gains and losses from sales of assets.

Cost of Goods Sold

Cost of goods sold includes buying and occupancy expenses.

Cash and Cash Equivalents

Cash and cash equivalents include temporary cash investments of $17,560,000 and $250,414,000 at December 31, 1992 and 1991, respectively, stated at cost, which approximates market. The Company considers all highly liquid investment instruments purchased with a remaining maturity of three months or less to be cash equivalents.

Inventories

Inventories are generally stated at the lower of cost, using the LIFO method, or market.

Depreciation and Amortization

Depreciation of buildings and equipment is based upon the estimated useful lives of these assets using the straight-line method. Amortization of capital leases, improvements to leased properties and favorable leaseholds is based upon the remaining terms of the leases or the estimated useful lives, whichever is shorter.

The fair value of future royalty payments from Japanese and other foreign and domestic licensees was recorded as a result of the application of purchase accounting pursuant to the Merger as discussed in Notes 2 and 7. The value of the royalties is being amortized using the straight-line method over 20 years, which is less than the estimated lives of the various royalty agreements, the majority of which are perpetual. Income is being recognized for royalty fees earned.

Income Taxes

Income taxes are the estimated amount of federal, foreign and state income taxes on earnings reported in the consolidated statements of operations. Deferred taxes and deferred tax benefits are provided for and are a result of timing differences between financial and tax reporting.

Leases

Capital leases are recorded at the inception of the lease at the lower of the discounted present value of future minimum lease payments or the fair value of the property.

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Store Closings

Provision is made on a current basis for the write-down of identified owned-store closings to their estimated net realizable value. For identified leased-store closings, provision is made on a current basis if anticipated expenses are in excess of expected sublease rentals.

Business Segment

The Company operates in a single business segment — the operating and franchising of convenience food stores, primarily under the 7-Eleven name.

2. Restructuring

On December 15, 1987, The Southland Corporation was acquired by JT Acquisition Corporation pursuant to a $4.9 billion leveraged buyout transaction and merger into the Company, with the Company continuing as the surviving corporation (the Merger). Subsequent to the Merger and through 1990, the Company sustained significant recurring losses. On October 24, 1990, The Southland Corporation filed a Voluntary Petition for Relief under Chapter 11 of Title 11 of the United States Code in the United States Bankruptcy Court (the Court). None of The Southland Corporation's subsidiaries were part of the Chapter 11 filing. The Southland Corporation also filed the Debtor's Plan of Reorganization (the Plan).

The significant features of the Plan, which occurred concurrently, consisted of a cash infusion of $430,000,000 from the sale of 286,634,619 shares of newly issued common stock, representing approximately 70% of the Company's outstanding shares, to IYG Holding Company (the Purchaser), renegotiations of the bank Credit Agreement (see Note 9), an agreement to refinance the Cityplace notes in 1995 (see Note 9), the cancellation of certain classes of old debt (the Old Debt Securities) and Redeemable Preferred Stock (collectively, the Old Securities) and the issuance of new debt (the Restructured Debt Securities), common stock warrants (Thompson Warrants) and/or payment of cash (collectively, the Restructuring) (see Note 9). The Thompson Warrants are exercisable from June 5, 1991, through February 23, 1996, for $1.75 per share against approximately one-half of the Thompsons' ownership. The Plan was confirmed by the Court and the Restructuring was consummated on March 5, 1991. As a result of the Restructuring, the Company is a majority-owned subsidiary of the Purchaser, which is jointly owned by Ito-Yokado Co., Ltd. (IY) and Seven-Eleven Japan Co., Ltd. Upon consummation of the Restructuring, the Company's common stock was beneficially owned approximately 70% by the Purchaser, 25% by holders of the Old Securities and 5% by the pre-Restructuring shareholders, which consisted primarily of the Thompson family and their affiliates. Subsequent to such time, the Purchaser's interest has declined to approximately 64% from private transactions of the Company's common stock in 1992.

The cancellation of the Old Debt Securities and the issuance of the Restructured Debt Securities and common stock to the holders of such Old Debt Securities resulted in an extraordinary gain in 1991 of $156,824,000. A portion of the gain is attributable to interest accrued on the Old Debt Securities that was not paid and was partially offset by the write-off of deferred costs associated with the Old Debt Securities, the costs incurred to issue the Restructured Debt Securities and a cash payment made to the holders of the Senior Extendible Reset Notes.

For each share of Redeemable Preferred Stock cancelled, the holders of such stock received one share of common stock, which resulted in a decrease in the accumulated deficit in 1991 of $127,788,000.

The balance sheet effects of noncash Restructuring transactions, which are not reflected in the Consolidated Statement of Cash Flows for the year ended December 31, 1991, are as follows (dollars in thousands):

Decrease in deposits and prepaid expenses	$ 19,186
Decrease in other assets	$ 50,289
Decrease in accounts payable and accrued expenses	$ 118,815
Net decrease in long-term debt	$ 280,951
Decrease in Redeemable Preferred Stock	$ 148,496
Increase in common stock and additional capital	$ 153,752
Decrease in accumulated deficit	$ 325,035

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3. Accounts and Notes Receivable

(Dollars in Thousands)	December 31 1992	1991
Notes receivable (net of long-term portion of $6,910 and $7,983)	$ 3,992	$ 4,590
Trade accounts receivable	89,945	79,886
Franchisee accounts receivable	49,338	54,552
	143,275	139,028
Allowance for doubtful accounts	(11,925)	(13,397)
	$ 131,350	$ 125,631

4. Inventories

Inventories stated on the LIFO basis which are included in inventories in the accompanying Consolidated Balance Sheets approximated $76,944,000 and $164,040,000 at December 31, 1992 and 1991, respectively, which is less than replacement cost by approximately $33,991,000 and $55,757,000, respectively. At December 31, 1992 and 1991, inventories were reduced resulting in a liquidation of LIFO inventory layers recorded at costs that were lower than the costs of current purchases. The effects of these reductions were to decrease the loss on the sale and closing of the distribution and food centers by approximately $23,000,000 in 1992 and decrease cost of goods sold by approximately $13,000,000 in 1991.

5. Property, Plant and Equipment

(Dollars in Thousands)	December 31 1992	1991
Cost:		
Land	$ 537,406	$ 591,221
Buildings and leaseholds	1,186,968	1,271,735
Machinery and equipment	543,616	613,682
Construction in process	13,704	13,495
	2,281,694	2,490,133
Accumulated depreciation and amortization	(925,531)	(897,867)
	$ 1,356,163	$ 1,592,266

6. Divested Assets & Discontinued Operations

Distribution & Food Center Assets

On November 30, 1992, the Company sold two of its five distribution centers and three of its six food centers, together with substantially all of the centers' inventories and receivables to McLane Company, Inc. (McLane). Through December 31, 1992, the Company has received cash proceeds of $141,800,000 and additional proceeds will be received in 1993 for the assets held for sale. In addition, two of the remaining distribution and food centers were closed in December 1992, and the third facility is scheduled to be closed in the first half of 1993. The Company intends to sell or sublease all of the remaining facilities at a future date.

Assets held for sale at December 31, 1992, primarily represent inventories to be sold to McLane in 1993 during the shut-down of the remaining facilities. The long-term assets remaining to be sold are recorded in property, plant and equipment at their estimated net realizable value. Liabilities relating to the assets to be sold in future years include accruals for operating leases, carrying costs and future capital expenditures.

The $45,000,000 pre-tax loss on the sale and closing of the distribution and food centers includes the loss from the sale of assets to McLane, the expected loss on future sales of the remaining facilities, and the expected net cash outflows on all such facilities subsequent to August 31, 1992 (the measurement date), until the expected dates of disposition. Operating results for the four-month period ended December 31, 1992, which were included in the loss, were not material.

In connection with the sale of assets to McLane, the Company and McLane have entered into a long-term service agreement under which McLane is making its distribution services available to 7-Eleven stores in the United States.

Cityplace Assets

On December 31, 1990, the Company sold its Cityplace real estate development excluding Cityplace Center East, its corporate office facility. The assets sold consisted of approximately 140 acres of primarily undeveloped land surrounding Cityplace Center East, located just north of the Dallas central business district. Sale proceeds were $24,000,000, and a loss of $41,000,000 was recognized in consolidated operating results for the year ended December 31, 1990.

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Citgo Operations

On January 31, 1990, the Company sold its 50% interest in the common stock of Citgo Petroleum Corporation (Citgo) to an affiliate of Petroleos de Venezuela, S.A., the state-owned oil company of Venezuela, for $661,500,000 in cash. The Company recognized a net loss of $1,070,000 in 1989, calculated as net proceeds less the book value of the investment and taxes of $205,813,000 that were recorded in January 1990.

The Company entered into a product purchase agreement with Citgo in 1986, which will expire in 2006, to buy specified quantities of gasoline at market prices. These prices are determined pursuant to a formula based on the prices posted by gasoline wholesalers in the various market areas where the Company purchases gasoline from Citgo. Minimum required annual purchases under this agreement are generally the lesser of 750,000,000 gallons or 35% of gasoline purchased by the Company for retail sale. The Company has exceeded the minimum required annual purchases both in the current year and in previous years. The Company expects to exceed the minimum required annual purchase levels.

7. Other Assets

(Dollars in Thousands)	December 31 1992	1991
Japanese license royalty (net of accumulated amortization of $84,941 and $68,926)	$ 233,559	$ 249,575
Other license royalties (net of accumulated amortization of $15,229 and $12,380)	41,540	44,389
Deferred debt issuance costs (net of accumulated amortization of $63,676 and $60,175)	9,567	11,564
Other (net of accumulated amortization of $3,543 and $4,449)	52,783	74,656
	$ 337,449	$ 380,184

8. Accounts Payable and Accrued Expenses

(Dollars in Thousands)	December 31 1992	1991
Trade accounts payable	$ 201,389	$ 243,729
Accrued insurance	87,422	101,167
Accrued payroll	61,550	75,906
Accrued taxes, other than income	45,334	52,919
Other	144,920	128,270
	$ 540,615	$ 601,991

Other includes accounts payable to The Southland Corporation Employees' Savings and Profit Sharing Plan (see Note 14) of $17,295,000 and $17,288,000 as of December 31, 1992 and 1991, respectively. Company contributions represented $14,371,000 and $14,135,000, respectively, of the total, and the remaining balances were primarily contingent rent payables.

9. Debt

(Dollars in Thousands)	December 31 1992	1991
Senior Term Loan due 1995	$ 237,938	$ 729,919
Commercial Paper	150,000	—
12% Senior Notes due 1996	370,890	400,962
5% First Priority Senior Subordinated Debentures due 2003	660,807	683,344
4½% Second Priority Senior Subordinated Debentures (Series A) due 2004	313,251	322,541
4% Second Priority Senior Subordinated Debentures (Series B) due 2004	27,505	28,258
12% Second Priority Senior Subordinated Debentures (Series C) due 2009	64,925	67,540
6¼% Yen Loan	291,162	305,441
7⅞% Cityplace Notes due 1995	285,238	283,304
12% Canadian Notes	—	34,284
Canadian revolving credit facility	7,388	7,833
Real estate and equipment notes and other debt with maturities through 2004 and a weighted average effective interest rate of 9.4%	14,182	26,311
Capital lease obligations	137,157	152,112
	2,560,443	3,041,849
Less long-term debt due within one year	152,515	168,246
	$ 2,407,928	$ 2,873,603

Bank Credit Agreement

At the time of the Merger in 1987, the Company became obligated under a Credit Agreement that presently includes a Senior Term Loan (Term Loan) and a revolving credit facility. At both December 31, 1992 and 1991,

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there were no borrowings outstanding under the revolving credit facility.

The Credit Agreement contains numerous financial and operating covenants requiring, among other things, the maintenance of certain financial ratios, including interest coverage, fixed-charge coverage and total debt. In addition, the Credit Agreement requires the attainment of certain levels of earnings before interest, income taxes and depreciation and amortization.

The Credit Agreement also contains various covenants which, among other things, (a) limit the Company's ability to incur indebtedness or other liabilities other than under the Credit Agreement, (b) restrict the Company's ability to engage in leasing transactions, (c) limit future capital expenditures and (d) restrict the Company's ability to pay cash dividends, redeem or prepay principal and interest on any subordinated debt and certain senior debt. Under the Credit Agreement, all of the assets of the Company, with the exception of certain specified property, serve as collateral.

Interest on the Term Loan and the revolving credit facility is generally payable quarterly and is based on a variable rate equal to the administrative agent bank's base rate plus 1.5% per year or, at the Company's option, at a rate equal to a reserve-adjusted Eurodollar rate plus 2.5% per year. The weighted average rate of bank debt outstanding at December 31, 1992, was 6.2%.

In September 1992, the Company entered into an amendment to the Credit Agreement that: (a) changed the financial covenants effective for June 30, 1992, through December 31, 1995, (b) extended the maturity of the Company's $275 million revolving credit facility through December 31, 1995, (c) required prepayments of $350 million on the Term Loan and (d) permitted the establishment of a $400 million commercial paper facility.

In accordance with the September amendment, $350 million in prepayments of the Term Loan were made in September. In addition, as a result of the sale of the distribution and food center assets (see Note 6) and in accordance with an October amendment to the Credit Agreement, a $110 million prepayment of the Term Loan was made on December 1, 1992. The $460 million in prepayments were applied to all remaining scheduled quarterly installments, reducing such quarterly installments to $12.5 million in 1993, $18.8 million in 1994, $42.9 million for the first two quarters of 1995 and $27.1 million upon maturity of the Term Loan on September 30, 1995.

As amended, the revolving credit facility makes available borrowings and letters of credit totaling a maximum of $275 million until its expiration on December 31, 1995. Maximum borrowings under the revolving credit facility, which are set at $150 million, are limited to $25 million whenever the face amount of commercial paper outstanding is below $375 million or the ratings of the commercial paper drop below certain levels. Upon expiration of the facility, all the then outstanding letters of credit may need to be replaced, and all other amounts then outstanding will be due and payable in full. At December 31, 1992, $140.1 million in letters of credit was outstanding. A fee of 2% per year on the outstanding amount of letters of credit is required to be paid. A ½% per year commitment fee on unadvanced funds, which for purposes of this calculation include outstanding letters of credit, is payable quarterly.

Commercial Paper Facility

In September, the Company obtained a facility that provides for the issuance of up to $400 million in commercial paper. Such debt is unsecured and is fully and unconditionally guaranteed by IY. At December 31, 1992, $150 million of the $221.9 million outstanding principal, net of discount, was classified as long-term debt since the Company intends to maintain at least this amount outstanding during the next year. In addition, IY intends to continue its guarantee of all commercial paper issued on or before December 31, 1993. While it is not anticipated that IY would be required to perform under its commercial paper guarantee, in the event IY makes any payments under the guarantee, the Credit Agreement prohibits the Company from reimbursing IY for the first $375 million of any such payments of principal made pursuant to the commercial paper guarantee. The Company is, however, allowed to reimburse IY for the remaining $25 million. The Company has entered into an agreement with IY under which it would not be required to reimburse IY for $375 million of such principal payments until one year after expiration of the Credit Agreement at which time reimbursement shall be immediately due. The weighted average interest rate on commercial paper borrowings outstanding at December 31, 1992, was 3.8%.

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Restructured Notes & Debentures

In accordance with the provisions of the Plan, upon consummation of the Restructuring, the Company issued five series of notes and debentures (Restructured Debt Securities), plus common stock and cash, and cancelled the Old Debt Securities (see Note 2). The Restructured Debt Securities were recorded in accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructuring", at an amount equal to the future undiscounted cash payments, both principal and interest. Accordingly, no interest expense will be recognized over the life of these securities, and cash interest payments (SFAS 15 Interest) will be charged against the recorded amount of such securities. Interest on all of the Restructured Debt Securities is payable in cash semiannually on June 15 and December 15 of each year.

The 12% Senior Notes, due December 15, 1996, were recorded at $446,070,000 with an aggregate principal amount of $250,601,000. They are currently redeemable at the option of the Company at 100% of principal amount.

The 5% First Priority Senior Subordinated Debentures, due December 15, 2003, were recorded at $717,151,000 with an aggregate principal amount of $450,755,000. They are redeemable at any time at the Company's option at 100% of principal amount. Annual sinking fund payments of $27,045,000 are due each December 15, commencing 1996 through 2002. These payments retire 42% of the debt before maturity.

The Second Priority Senior Subordinated Debentures were issued in three series. Each series is redeemable at any time at the Company's option at 100% of principal amount.

— 4.5% Series A Debentures, due June 15, 2004, were recorded at $336,474,000, with an aggregate principal amount of $206,426,000.

— 4% Series B Debentures, due June 15, 2004, were recorded at $29,389,000, with an aggregate principal amount of $18,839,000.

— 12% Series C Debentures, due June 15, 2009, were recorded at $70,808,000, with an aggregate principal amount of $21,787,000.

The Restructured Debt Securities contain certain covenants which, among other things, (a) limit the payment of dividends and certain other restricted payments by both the Company and its subsidiaries, (b) require the purchase by the Company of the Restructured Debt Securities at the option of the holder upon a change of control, (c) limit additional indebtedness, (d) limit future exchange offers, (e) limit the repayment of subordinated indebtedness, (f) require board approval of certain asset sales, (g) limit transactions with certain stockholders and affiliates and (h) limit consolidations, mergers and the conveyance of all or substantially all of the Company's assets.

The Senior Notes are unsecured senior obligations of the Company. The First and Second Priority Senior Subordinated Debentures are subordinate to the bank loans outstanding under the Credit Agreement, to the Senior Notes and to previously outstanding mortgages and notes that are backed by specific collateral or are general unsecured, unsubordinated obligations. The Second Priority Debentures are subordinate to the First Priority Debentures.

Other Debt

In March 1988, the Company monetized its future royalty payments from the area licensee in Japan, Seven-Eleven Japan Co., Ltd., through a loan that is nonrecourse to the Company as to principal and interest. The debt, payable in Japanese yen, was in the amount of 41 billion yen, or approximately $327,000,000, and is collateralized by the Japan trademarks and a pledge of the future royalty payments (see Note 1). The current interest rate of 6¼% will be reset after March 1998. Payment of the debt is required no later than March 2006 through future royalties from the Japanese licensee, and the Company believes it is remote that there will be any principal balance remaining at that date. The Company has hedged the loan by designating its future royalty receipts, during the term of the loan, to service the monthly interest and principal payments, thus offsetting the impact of future exchange rate fluctuations.

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Cityplace Center East Corporation (CCEC), a subsidiary of the Company, issued $290,000,000 of notes in March 1987 to finance the construction of the headquarters tower, a parking garage and related facilities of the Cityplace Center development. These notes bear interest at 7⅞%, payable semiannually on February 15 and August 15, with the principal amount due February 15, 1995. After the application of purchase accounting pursuant to the Merger in 1987, the effective interest rate on the notes for financial statement purposes is 9.0%. Principal and interest on the notes are payable by drawings under irrevocable letters of credit issued by The Sanwa Bank, Limited, Dallas Agency (Sanwa), which, along with the note holders, has been granted a lien on the property financed. The Company is occupying a portion of the building as its corporate headquarters and is attempting to sublease the rest. On December 21, 1990, the Company and CCEC entered into an amendment to the agreement with Sanwa, which became effective upon consummation of the Restructuring. It provides that, upon maturity of the notes in February 1995, the noteholders will draw on the letter of credit in payment of their principal. At such time, the Company has the option of either repaying the principal to Sanwa or extending the term of maturity ten years to March 1, 2005, with monthly payments of principal and interest based upon a 25-year amortization at 7½%, with the remaining principal due upon maturity. As additional consideration, CCEC will pay to the lender any net sublease income it receives on the property and 60% of the proceeds less $275 million and permitted costs upon a sale or refinancing of the building.

In July 1985, Southland Canada, Inc., an indirect wholly owned subsidiary of the Company, issued 12% Canadian notes with a face amount of Canadian $50,000,000. On July 25, 1992, these notes matured and all principal and interest outstanding was repaid.

During 1988, Southland Canada, Inc. entered into a revolving credit facility with a Canadian chartered bank. The facility currently provides bank financing of up to Canadian $21,429,000 (approximately U.S. $16,854,000 at December 31, 1992), which will be reduced to Canadian $17,858,000 on June 30, 1993, and will be further reduced each year thereafter until June 30, 1998, when the facility will expire, and all amounts outstanding will be due and payable in full. At December 31, 1992, the Company had borrowings outstanding under this facility of Canadian $9,393,000 (approximately U.S. $7,388,000). Interest on such facility is generally payable monthly and is based upon the Canadian Prime rate (7.25% at December 31, 1992) plus .5% per year.

As of December 31, 1992, long-term debt maturities, which include capital lease obligations and sinking fund requirements, as well as SFAS 15 Interest accounted for in the recorded amount of the Restructured Debt Securities, are as follows (dollars in thousands):

1993	$ 152,515
1994	176,671
1995	215,028
1996	390,150
1997	116,220
Thereafter	1,509,859
	$ 2,560,443

10. Redeemable Preferred Stock

In connection with the Merger in 1987, the Company issued 9,911,656 shares of Junior Preferred Stock, 15% Cumulative Exchangeable Preferred Stock, Series One (the Redeemable Preferred Stock), with a $25 liquidation preference per share. Dividend payments made in additional shares through March 15, 1990, resulted in the issuance of 3,893,439 new shares, for a total of 13,805,095 shares. In accordance with the provisions of the Plan, upon consummation of the Restructuring, each share of Redeemable Preferred Stock was cancelled and holders thereof received one share of common stock and .073 Thompson Warrants (see Note 2).

11. Preferred Stock

The Company has 5,000,000 shares of another class of preferred stock authorized for issuance. Any preferred stock issued will have such rights, powers and preferences as determined by the Company's Board of Directors.

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12. Redeemable Common Stock Purchase Warrants

In connection with the Merger in 1987, the Company issued 26,135,682 redeemable common stock purchase warrants (the Warrants). The Warrants were recorded at $1.00 per Warrant, which was the amount of proceeds allocated to the Warrants at the time of issuance. The Warrants were governed by a Warrant Agreement and were exercisable through December 15, 1992, only upon the occurrence of certain specified events. None of the specified events occurred on or before December 15, 1992, and all of the warrants expired on December 16, 1992. Under the provisions of the Warrant Agreement, the Company was obligated to repurchase the Warrants by March 15, 1995 at the fair market value of the Warrants as separate securities, as determined by an independent financial expert. A fair market value of $0 for the Warrants was determined by an independent financial expert in December 1992. The $26,135,682 difference between the carrying amount of the Warrants and their fair value was recorded as an increase in additional capital in 1992.

13. Disclosures About Fair Value of Financial Instruments

The following disclosure of the estimated fair value of financial instruments is made in accordance with SFAS No. 107, "Disclosures about Fair Value of Financial Instruments". The estimated fair value amounts have been determined by the Company, using available market information and appropriate valuation methodologies.

The carrying amounts of Cash and Cash Equivalents, Trade Accounts Receivable and Trade Accounts Payable are reasonable estimates of their fair values. Letters of credit are included in the estimated fair value of Trade Accounts Payable. The estimated fair values of other financial instruments at December 31, 1992, are listed in the following table.

(Dollars in Thousands)	**Carrying Amount**	**Estimated Fair Value**
Bank Debt	$ 237,938	$ 237,938
Commercial Paper	221,866	221,866
Restructured Notes and Debentures	1,437,378	648,305
Cityplace Notes	285,238	301,238
Yen Loan	291,162	295,117

The methods and assumptions used in estimating the fair value for each of the classes of financial instruments presented in the table above are as follows:

The carrying amount of the bank debt under the Credit Agreement approximates fair value because the interest rate is variable.

Commercial paper borrowings were sold at market interest rates and have an average maturity of less than 18 days. Therefore, the carrying amount of commercial paper is a reasonable estimate of its fair value. The guarantee of the commercial paper by IY is an integral part of the estimated fair value of the commercial paper borrowings.

The fair values of the Restructured Debt and the Cityplace Notes were estimated based upon December 31, 1992, bid prices obtained from investment banking firms where traders regularly make a market for these financial instruments. The carrying amount of the Restructured Debt includes $488,970,000 of SFAS 15 Interest (see Note 9).

The fair value of the Yen Loan was estimated by calculating the present value of the future yen cash flows at current interest and exchange rates.

14. Employee Benefit Plans

Employees' Savings and Profit Sharing Plan

Effective January 1, 1949, the Company adopted The Southland Corporation Employees' Savings and Profit Sharing Plan (Savings and Profit Sharing Plan) for the purpose of providing retirement benefits for eligible employees.

Contributions to the Savings and Profit Sharing Plan are made by both the participants and the Company. The Company contributes the greater of approximately 10% of its net earnings before contribution to the Savings and Profit Sharing Plan and federal income taxes or an amount determined by the Company's president.

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The Company contribution is generally allocated to the participants on the basis of their individual contribution, years of participation in the Savings and Profit Sharing Plan and age. The Company contributions for the years ended December 31, 1992, 1991 and 1990 were $14,647,000 (including amounts allocated to the distribution and food centers), $14,411,000 and $13,653,000, respectively.

Postretirement Insurance Benefits

The Company's group insurance plan (the Insurance Plan) provides postretirement medical and dental benefits for all retirees that meet certain criteria. Such criteria include continuous participation in the Insurance Plan ranging from 10 to 15 years depending on hire date, and the sum of age plus years of continuous service equal to at least 70. The Company contributes toward the cost of the Insurance Plan a fixed dollar amount per retiree based on age and number of dependents covered, as adjusted for actual claims experience. All other costs and cost increases will be paid by the retirees. The Company continues to fund its cost on a cash basis; therefore, no plan assets have been accumulated.

During 1990, the Company adopted SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions". In accordance with the provisions of SFAS No. 106, the Company calculated accumulated postretirement medical and dental benefit obligations of $27,163,000 as if effective January 1, 1990. The obligation represents the actuarial present value, at a 9% weighted average discount rate, of postretirement benefits to be paid to current employees and retirees based on services rendered. The accumulated postretirement benefit obligation of $27,163,000 was recorded as the cumulative effect of an accounting change in the consolidated statement of operations for the year ended December 31, 1990.

Net periodic postretirement benefit costs recognized in earnings for 1992 and 1991 include the following components:

(Dollars in Thousands)	1992	1991
Service cost	$ 862	$ 1,298
Interest cost	1,998	2,679
Amortization of unrecognized gain	(564)	—
	$ 2,296	$ 3,977

The accrual for postretirement medical and dental benefits was reduced by approximately $3,883,000 during the fourth quarter of 1992 due to the termination of employees not eligible to retire. The weighted-average discount rate used in determining the accumulated postretirement benefit obligation was 8% and 9% at December 31, 1992 and 1991, respectively. Components of the accrual recorded in the Company's consolidated balance sheets as of December 31 are:

(Dollars in Thousands)	1992	1991
Accumulated Postretirement Benefit Obligation:		
Retirees	$ 12,757	$ 13,197
Active employees eligible to retire	5,636	2,384
Other active employees	7,377	6,817
	25,770	22,398
Unrecognized gains	1,693	7,878
	$ 27,463	$ 30,276

Postemployment Benefits

In November 1992, the Financial Accounting Standards Board issued SFAS No. 112, "Employers' Accounting for Postemployment Benefits". The statement requires recognition of an obligation for all benefits provided by an employer to former or inactive employees after employment but before retirement (postemployment benefits) and must be adopted no later than 1994. As defined in the statement, "postemployment benefits include, but are not limited to, salary continuation, supplemental unemployment benefits, severance benefits, disability-related benefits (including workers' compensation), job training and counseling, and continuation of benefits such as health care and life insurance coverage". The Company has not completed its review of the requirements of the statement and therefore has not determined the impact on earnings in the year of adoption. The Company has not yet decided when it will adopt the statement.

Equity Participation Plan

During 1988, the Company adopted The Southland Corporation Equity Participation Plan, which provides for the granting of both incentive options and nonstatutory options and the sale of convertible debentures to certain

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key employees and officers of the Company. The options were granted at the fair market value on the date of grant, which is the same as the conversion price provided in the debentures.

All options expire, and the debentures mature, no later than December 31, 1997. Options are not exercisable, and the debentures are not convertible, until the earlier of December 31, 1994, or until the occurrence of certain specified events set forth in the Plan. The Plan was amended to exclude the Restructuring from qualifying as such an event. In the aggregate, not more than 3,529,412 shares of common stock of the Company can be issued pursuant to the Plan; however, the Company has no present intention of granting additional options. At December 31, 1992, there were options outstanding to acquire 1,899,906 shares, of which 1,796,656 were at $7.50 per share and 103,250 were at $7.70 per share, and debentures outstanding that were convertible into 21,667 shares, none of which are currently exercisable or convertible.

Grant Stock Plan

During 1988, the Company adopted The Southland Corporation Grant Stock Plan (the Plan). Under the provisions of the Plan, up to 750,000 shares of common stock are authorized to be issued to certain key employees and officers of the Company. The stock was fully vested upon the date of issuance. As of December 31, 1992, 480,844 shares had been issued pursuant to the Plan; however, the Company has no present intention of granting additional shares. No shares have been issued since 1988. The shares available for issuance under the Equity Participation Plan are reduced by the number of shares issued under this Plan.

15. Leases, Commitments and Contingencies

Certain of the property, plant and equipment used in the Company's business is leased. Generally, real estate leases are for primary terms from 14 to 20 years with options to renew for additional periods, and equipment leases are for terms from one to ten years. The leases do not contain restrictions that have a material effect on the Company's operations.

The composition of capital leases reflected as property, plant and equipment in the consolidated balance sheets is as follows:

(Dollars in Thousands)	December 31 1992	December 31 1991
Buildings	$ 141,452	$ 152,692
Equipment	482	1,268
	141,934	153,960
Accumulated amortization	(63,880)	(61,949)
	$ 78,054	$ 92,011

The present value of future minimum lease payments for capital lease obligations is reflected in the consolidated balance sheets as long-term debt. The amount representing imputed interest necessary to reduce net minimum lease payments to present value has been calculated generally at the Company's incremental borrowing rate at the inception of each lease.

Future minimum lease payments for years ending December 31 are as follows:

(Dollars in Thousands)	Capital Leases	Operating Leases
1993	$ 27,759	$ 123,655
1994	26,831	113,554
1995	25,531	104,128
1996	24,157	95,028
1997	22,330	83,025
Thereafter	119,264	346,580
Future minimum lease payments	245,872	$ 865,970
Estimated executory costs	(850)	
Amount representing imputed interest	(107,865)	
Present value of future minimum lease payments	$ 137,157	

Minimum noncancelable sublease rentals to be received in the future, which are not included above as offsets to future payments, total $27,840,000 for capital leases and $31,342,000 for operating leases.

Rent expense on operating leases in the years ended December 31, 1992, 1991 and 1990, totaled $135,657,000, $140,294,000 and $138,138,000, respectively, including contingent rentals of $9,037,000, $9,738,000 and $9,587,000, but reduced by sublease rentals of $8,252,000, $8,270,000 and $7,776,000. Contingent rent expense on capital leases in the years ended December 31, 1992, 1991 and 1990, was $3,964,000, $5,067,000 and $4,947,000, respectively. Contingent rentals are generally based upon sales levels or changes in the Consumer Price Index.

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Leases With Savings and Profit Sharing Plan

At December 31, 1992, the Savings and Profit Sharing Plan owned 352 stores leased to the Company under capital leases and 663 stores leased to the Company under operating leases at rentals which, in the opinion of management, approximated market rates at the date of lease. During 1990, the Savings and Profit Sharing Plan purchased 10 stores from the Company. In addition, 31, 15 and 16 properties were sold to third parties in 1992, 1991 and 1990, respectively, and at the same time, the related leases with the Company were cancelled. Included in the consolidated financial statements are the following amounts related to leases with the Savings and Profit Sharing Plan which were in effect as of and for the year ended:

(Dollars in Thousands)	December 31 1992	1991
Buildings (net of accumulated amortization of $9,648 and $9,091)	$ 6,550	$ 8,497
Capital lease obligations (net of current portion of $2,302 and $2,412)	$ 9,184	$ 11,941

(Dollars in Thousands)	Years Ended December 31 1992	1991	1990
Rent expense under operating leases and amortization of capital lease assets, included in cost of goods sold	$ 29,210	$ 31,731	$ 31,007
Imputed interest expense on capital lease obligations	$ 1,213	$ 1,440	$ 1,826
Capital lease principal payments included in principal payments under long-term debt agreements	$ 2,302	$ 2,457	$ 2,504

Contingencies

The Company accrues future costs, net of related probable state reimbursement amounts, for remediation of gasoline store sites where releases of regulated substances have been detected. At December 31, 1992, the Company's estimated net liability for sites where releases have been detected was $0 as the estimated future remediation costs of between $45,000,000 and $60,000,000 are expected to be more than completely offset by the sum of estimated probable state reimbursements of these future costs as well as remediation costs incurred prior to December 31, 1992. The Company has not recorded the net receivable, however, as management does not believe realization of this amount is assured beyond a reasonable doubt. The estimated future remediation expenditures and related state reimbursement amounts could change as governmental requirements and state reimbursement programs are more fully defined.

The Company anticipates that substantially all of the future remediation costs for sites with detected releases of regulated substances at December 31, 1992, will be incurred within the next three years. There is no assurance of the timing of the receipt of state reimbursement funds. However, based on the Company's experience, the Company expects to receive state reimbursement funds within one to two years after incurring eligible remediation expenses, assuming that the states have developed the necessary procedures for implementing the reimbursement programs.

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16. Income Taxes

The components of the Loss Before Income Taxes (Benefit), Extraordinary Items and Cumulative Effect of Accounting Change are as follows:

	Years Ended December 31		
(Dollars in Thousands)	**1992**	**1991**	**1990**
Domestic	$ (113,940)	$ (58,039)	$ (434,435)
Foreign	(6,009)	(8,309)	4,479
Total	$ (119,949)	$ (66,348)	$ (429,956)

The provision (benefit) for federal and other income taxes are as follows:

	Years Ended December 31		
(Dollars in Thousands)	**1992**	**1991**	**1990**
Currently payable:			
Federal	$ 4,560	$ —	$ 13,941
Foreign	5,411	7,936	8,554
State	1,529	64	2,819
	11,500	8,000	25,314
Taxes on disposal of equity interest in Citgo	—	—	(205,813)
Tax benefit from utilization of net operating loss carryforwards	—	—	52,040
Income taxes (benefit)	$ 11,500	$ 8,000	$ (128,459)

The $128,459,000 income tax benefit in 1990 represents the benefit derived from the use of the 1990 loss from continuing operations to offset taxes provided on the disposal of the Company's equity interest in Citgo.

Reconciliations of taxes at the federal statutory rate to the Company's actual taxes provided are as follows:

	Years Ended December 31		
(Dollars in Thousands)	**1992**	**1991**	**1990**
Taxes (benefit) at federal statutory rate	$ (40,783)	$ 30,762	$ (85,444)
State income taxes, net of federal income tax benefit	1,009	42	1,861
Foreign taxes	5,411	7,936	8,554
Loss providing no current benefit	5,061	200,991	74,759
Amortization of cost in excess of tax basis	23,286	19,383	22,871
Tax benefit from utilization of net operating loss carryforwards	—	—	(52,040)
Difference in basis of assets sold	—	—	46,184
Portion of gain on debt restructuring not recognized for tax	—	(261,568)	—
Difference in LIFO as a result of purchase accounting	8,671	5,248	(143)
Equity in affiliates	3,148	3,966	(335)
Other	5,697	1,240	9,047
	$ 11,500	$ 8,000	$ 25,314

At December 31, 1992, the Company had tax general business credit carryforwards of $14,405,000 which expire during the period from 2001 to 2007, and alternative minimum tax credit carryforwards of $17,701,000 which have no expiration date.

Significant timing differences between financial and tax reporting amounts include the use of accelerated depreciation for tax purposes and nondeductible insurance accruals. However, the Company had no deferred taxes at December 31, 1992 or 1991, and had accumulated a book net operating loss (NOL) carryforward. This book NOL will not be carried forward because the Company will adopt SFAS No. 109, "Accounting for Income Taxes," as of January 1, 1993. The Company estimates that there will be no cumulative effect on earnings upon adoption of SFAS No. 109 because it will record a net deferred tax asset, which will be fully reserved.

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17. Earnings (Loss) Per Common Share

Primary earnings (loss) per common share is based on net earnings (loss) reduced (increased) by preferred stock dividends and accretion to redemption value of the Redeemable Preferred Stock and the Warrants, divided by the average number of shares, including the Warrants (unless the effect of considering the Warrants is antidilutive), outstanding during each year.

Earnings (loss) per share assuming full dilution is antidilutive and, therefore, is computed on the same basis as primary earnings (loss) per common share.

18. Quarterly Financial Data (Unaudited)

Summarized quarterly financial data for 1992 and 1991 is as follows:

Year Ended December 31, 1992:

(Dollars in Millions, Except Per-Share Data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Net sales	$ 1,763	$ 1,961	$ 1,988	$ 1,714	$ 7,426
Gross profit	352	422	445	386	1,605
Income taxes (benefit)	1	1	12	(2)	12
Net loss	(45)	(18)	(39)	(29)	(131)
Primary and fully diluted loss per common share	(.11)	(.04)	(.10)	(.07)	(.32)

The second quarter includes $17,500,000 of expense resulting from a cost cutting program associated with the Company's internal reorganization. The third and fourth quarters include losses of $41,000,000 and $4,000,000, respectively, relating to the sale and closing of the distribution and food centers (see Note 6). In addition, the fourth quarter includes a loss of $25,000,000 related to store closings and divestitures in 1992 or planned for 1993.

Year Ended December 31, 1991:

(Dollars in Millions, Except Per-Share Data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Net sales	$ 1,867	$ 2,109	$ 2,133	$ 1,901	$ 8,010
Gross profit	364	442	451	400	1,657
Income taxes	—	—	6	2	8
Earnings (loss) before extraordinary item	(53)	7	6	(34)	(74)
Net earnings (loss)	90	20	6	(34)	82
Primary and fully diluted earnings (loss) per common share before extraordinary item	(.39)	.02	.01	(.08)	(.22)

The first and second quarters include a gain on the debt restructuring of $143,824,000 and $13,000,000, respectively, (see Note 2). The fourth quarter includes a LIFO credit of approximately $16,000,000 primarily due to a decrease in inventory levels and a charge of approximately $12,000,000 for additional interest awarded under the Credit Agreement in a March 17, 1992, decision of the Bankruptcy Court.

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To the Board of Directors and Shareholders of
The Southland Corporation
Dallas, Texas

We have audited the accompanying consolidated balance sheet of The Southland Corporation and Subsidiaries as of December 31, 1992, and the related consolidated statements of operations, shareholders' equity (deficit) and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The consolidated financial statements of the Company as of December 31, 1991, and for the years ended December 31, 1991 and 1990, were audited by other auditors whose report dated March 27, 1992, included an explanatory paragraph that described the change in method of accounting for postretirement benefits other than pensions discussed in Note 14 to the financial statements.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Southland Corporation and Subsidiaries as of December 31, 1992, and the consolidated results of their operations and their cash flows for the year then ended in conformity with generally accepted accounting principles.

Coopers & Lybrand

Dallas, Texas
March 8, 1993

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DIRECTORS

Masatoshi Ito
Chairman;
Founder, Director and Advisor
of Ito-Yokado Group

Toshifumi Suzuki (1)
Vice Chairman;
President and Chief Executive Officer,
Ito-Yokado Co., Ltd;
Chairman and Chief Executive Officer,
Seven-Eleven Japan Co., Ltd.

John P. Thompson (1)
Co-Vice Chairman;
formerly Chairman,
The Southland Corporation

Jere W. Thompson
Co-Vice Chairman;
formerly President and
Chief Executive Officer,
The Southland Corporation

Clark J. Matthews, II
President and
Chief Executive Officer,
The Southland Corporation

Yoshitami Arai
Chairman,
Systems International, Inc.

Timothy Ashida (1)
President,
A.K.K. Associates, Inc.

Jay W. Chai (2)
Chairman and
Chief Executive Officer,
ITOCHU International Inc.

Gary J. Fernandes (2)
Senior Vice President and
Director, Electronic Data
Systems Corporation

Masaaki Kamata
Executive Vice President,
Seven-Eleven Japan Co., Ltd.

Kazuo Otsuka (1)
General Manager,
Corporate Development,
Ito-Yokado Co., Ltd.

Asher O. Pacholder (2)
Chairman and Managing Director,
Pacholder Associates, Inc.

Walter J. Salmon (2)*
Professor,
Senior Associate Dean and
Director, External Relations,
Harvard Business School

Nobutake Sato
Senior Managing Director,
Corporate Planning,
Ito-Yokado Co., Ltd.

Joe C. Thompson, Jr.**
Chairman,
Sigel Liquor Stores, Inc.

(1) Compensation and Benefits Committee
(2) Audit Committee

* Not standing for re-election in 1993; Tatsuhiro Sekine, Managing Director, Financial Department and Information Systems Management, Ito-Yokado Co., Ltd., has been nominated for his seat

** Resigned December 30, 1992

OFFICERS

Masatoshi Ito
Chairman of the Board

Toshifumi Suzuki
Vice Chairman of the Board

Clark J. Matthews, II
President
and Chief Executive Officer

Stephen B. Krumholz
Senior Vice President,
Operations

John H. Rodgers
Senior Vice President,
Chief Administrative Officer
and Secretary

Rodney A. Brehm
Vice President,
Merchandising

Adrian O. Evans
Vice President,
Construction and Maintenance

David M. Finley
Vice President,
Human Resources

James W. Keyes
Vice President,
Planning and Finance

Stephen B. LeRoy
Vice President,
Real Estate and Licensed Operations

Vernon P. Lotman
Vice President and
Controller

Cecilia Stubbs Norwood
Vice President,
Corporate Communications

Michael K. Roemer
Vice President,
Line Management

Bryan F. Smith, Jr.
Vice President and
General Counsel

David A. Urbel
Vice President, Strategic Planning,
and Treasurer

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Corporate Headquarters

The Southland Corporation
2711 North Haskell Ave.
Dallas, TX 75204-2906
(214) 828-7011

Mailing Address:
P.O. Box 711
Dallas, TX 75221-0711

Form 10-K and Other Investor Information

Requests for the Form 10-K for the year ended December 31, 1992, and quarterly financial information should be addressed to the Investor Relations Manager at the above address, or telephone (214) 828-7209.

Annual reports are automatically mailed to all shareholders. Investors may automatically receive quarterly information by requesting to be put on the company's mailing list.

A recorded company update can be reached and requests for information can be left 24 hours a day by calling (214) 828-7587.

Annual Meeting

The annual meeting will be held at 9:30 a.m. CDT on Wednesday, April 28, 1993, in the Cityplace Conference Center at the company's headquarters. All shareholders and bondholders are cordially invited to attend.

Auditors

Coopers & Lybrand
Dallas, Texas

Common Stock Transfer Agent/Registrar

Society National Bank
c/o Society Shareholder Services, Inc.
P.O. Box 2320
Dallas, Texas 75221-2320
From All Locations: 1-800-527-7844

Common Stock

Southland's common stock is traded on the Nasdaq Small-Cap Market under the ticker symbol SLCMC. The stock is listed as "SouldCp h" in the Nasdaq Small-Cap chart of most major daily newspapers. There were 3,373 shareholders of record as of December 31, 1992.

The stock was issued on March 5, 1991, as part of Southland's restructuring. The company has not paid any dividends on its common equity since that time, and dividend payments are restricted by the indentures governing the company's outstanding securities and Southland's senior credit agreement.

The tables below set forth the high, low and closing bid prices for the periods indicated as provided by Nasdaq. These quotations reflect inter-dealer prices without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

	PRICE RANGE (BID)		
QUARTERS	**HIGH**	**LOW**	**CLOSE**
1992			
FIRST	\$ 2 3/8	\$ 1 11/16	\$ 2 1/32
SECOND	2 1/32	1 1/4	1 3/4
THIRD	4 3/16	1 1/4	3 11/16
FOURTH	3 11/16	2 13/16	3
1991			
FIRST	\$ 2 21/32	\$ 1/2	\$ 2 9/32
SECOND	2 21/32	1 5/8	1 25/32
THIRD	2 13/32	1 25/32	2 5/32
FOURTH	3 1/16	1 7/8	1 7/8

Other Securities

The following other Southland securities are traded over the counter, and reported bond price information (updated Fridays) is available by calling the company's recorded message at (214) 828-7587:

12% Senior Notes due 1996
5% First Priority Senior Subordinated Debentures due 2003
4.5% Second Priority Senior Sub. Debs. (Series A) due 2004
4% Second Priority Senior Sub. Debs. (Series B) due 2004
12% Second Priority Senior Sub. Debs. (Series C) due 2009

Common Stock Warrants (expire 2/23/96; exercisable at \$1.75 per share)

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United States

Franchised	3,011
Company-operated	2,662

Canada

Company-operated	494 (1)
	6,167

Licensed or Operated by Affiliates (2)

Japan(3)	4,974
Taiwan	709
United States	641
Hong Kong	284
Australia	181
Mexico	158
Thailand	158
Malaysia	86
Singapore	67
Spain	66
South Korea	56
United Kingdom	52
Sweden	37
Philippines	35
Norway	29
Brazil	14
Puerto Rico	13
Turkey	12
Panama	8
Guam	5
China	5
Virgin Islands	3
	7,593
	13,760

(1) The number of company-operated stores in Canada includes 17 locations in which Southland has no real estate interest.

(2) Sales from stores operated by licensees or affiliates are not included in Southland's "Net Sales." Royalties from licensees and equity in affiliates are included in "Other Income."

(3) The 7-Eleven licensee in Japan, Seven-Eleven Japan Co., Ltd., and its parent company, Ito-Yokado Co., Ltd., jointly own IYG Holding Company, which owns 64% of Southland's common stock.

State/Province	7-Eleven Stores	Other Retail	Total
United States:			
Arizona	107	0	107
California	1,224	5	1,229
Colorado	256	0	256
Connecticut	39	0	39
Delaware	29	0	29
District of Columbia	19	2	21
Florida	521	0	521
Idaho	14	0	14
Illinois	158	11	169
Indiana	17	4	21
Kansas	20	0	20
Maryland	321	53	374
Massachusetts	35	2	37
Michigan	100	0	100
Missouri	93	2	95
Nevada	187	0	187
New Hampshire	8	4	12
New Jersey	211	0	211
New Mexico	22	0	22
New York	217	0	217
North Carolina	8	0	8
Ohio	16	0	16
Oregon	141	0	141
Pennsylvania	173	9	182
Rhode Island	9	0	9
Texas	477	3	480
Utah	134	0	134
Virginia	652	44	696
Washington	275	0	275
West Virginia	20	14	34
Wisconsin	0	17	17
Canada:			
Alberta	130	0	130
Manitoba	55	0	55
Ontario	128	0	128
British Columbia	142	0	142
Saskatchewan	39	0	39
Total	5,997	170	6,167

All numbers as of December 31, 1992

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